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Vol. I

TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1935

No. 17

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES OF AN EXPRESS TRUST KNOWN AS WESTERN AVENUE GOLF CLUB, PETITIONERS,

vs.

COMMISSIONER OF INTERNAL REVENUE.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

PETITION FOR CERTIORARI FILED APRIL 1, 1935.

CERTIORARI GRANTED MAY 13, 1935.

SUPREME COURT OF THE UNITED STATES

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VOL. I.

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APPEARANCES.

For Taxpayer:
THEODORE B. BENSON, ESQ.,
JAMES C. O'BRIEN, ESQ.,

For Comm'r.:
J. M. LEINENKUGEL, ESQ.,

DOCKET ENTRIES.

1928

Oct. 11—Petition received and filed. Taxpayer notified. (Fee paid)

" 12—Copy of petition served on General Counsel.

Nov. 30—Answer filed by General Counsel.

Dec. 1—Copy of answer served on taxpayer. General Calendar.

1929

Oct. 17—Motion to consolidate for hearing on Oct. 23, 1929 with docket 34[illegible]led by taxpayer.

" 17—Motion to leave to amend petition embodying amendment filed by taxpayer. 10/21/29 granted.

" 21—Motion to withdraw motion to consolidate filed by taxpayer. 10/21/29 granted.

" 23—Copy of motion and amendment served on General Counsel.

Dec. 19—Answer to amendments to petition filed by General Counsel. 12/20/29 copy served.

1930

Jan. 14—Hearing set 3/6/30.

Mar. 3—Motion to consolidate with 34287 for hearing filed by General Counsel. See 34287—no action.

" 5—Motion to consolidate with 34287 for hearing and place on Reserve Calendar filed by taxpayer.

" 6—Motion granted.

May 11—Motion to continue to Circuit Calendar for hearing in Los Angeles and consolidate with 34287 filed by taxpayer. 5/6/31 granted to Circuit Hearing.

1932

Apr. 14—Hearing set for June 6, 1932 in Los Angeles, California.

Jun. 6-10—Hearing had before Mr. Smith, Div. 5 on the merits. Submitted. Amended answer allowed—served—30 days for reply stipulation of facts filed at hearing—briefs due in 60 days.

Jul. 7—Motion for extension of 15 days to file reply to amended answer filed by taxpayer. 7/18/32 granted.

Aug. 4—Motion for extension to Oct. 9, 1932 to to file brief filed by General Counsel. 8/5/32 granted both sides.

Oct. 6—Motion for extension of 60 days to file brief filed by General Counsel. 10/7/32 granted to 12/1/32 to both sides.

Nov. 4—Brief filed by General Counsel.

Dec. 5—Transcript of hearing of Jun 10, 1932 filed. [1*]

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*Page numbering appearing at the foot of page of original certified Transcript of Record.

1933

Jan. 12—Proposed findings of fact and brief filed by taxpayer.

Mar. 24—Memorandum opinion rendered, Mr. Smith, Div. 5. Judgment will be entered under Rule 50.

May 24—Notice of settlement filed by General Counsel.

" 27—Hearing set June 21, 1933 on settlement.

Jun. 21—Hearing had before Mr. Van Fossan on settlement. Referred to Mr. Smith for decision.

" 23—Decision entered, Charles P. Smith, Div. 5.

Sep. 23—Petition for review by U. S. Circuit Court of Appeals (9) with assignments of error filed by taxpayer.

" 23—Proof of service filed by taxpayer.

Nov. 16—Praecipe filed. Proof of service thereon.

" 21—Order enlarging time to Dec. 30, 1933 to file certified copies of record papers sur petition for review entered. [2]

VOL. I

The United States Board of Tax Appeals

Docket No. 40977

T, A. MORRISSEY and JAMES M. O'BRIEN, Trustees of an Express Trust, known as Western Avenue Golf Club,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency IT:AR:A-5-NMP dated August 20, 1928, and as a basis of their proceedings allege as follows:

1. The petitioners are trustees of an express trust known as Western Avenue Golf Club with the principal place of business at 824 Van Nuys Building, City of Los Angeles, State of California.

2. The notice of deficiency (a copy of which is attached hereto, made a part hereof and marked Exhibit "A") was mailed by the Commissioner of Internal Revenue August 20, 1928, and alleges a deficiency for the years 1924 to 1926, inclusive, in the amount of $8,518.12. [3]

3. The tax in controversy is the income tax for the calendar years 1924 to 1926, inclusive, and the

amount thereof is less than $10,000.00, to wit: $8,518.12.

4. The determination of tax set forth in the said notice of deficiency is based on the following errors:

(a) The Commissioner of Internal Revenue erroneously determined that the declaration of trust under which the petitioners are trustees created an "association" within the meaning of Section 2 of the Revenue Acts of 1924 and 1926, and as a result thereof the said Commissioner determined the net income and computed the tax in the manner and at the rates set forth in Part II of the said Revenue Acts, whereas in law and fact the declaration of trust did not create such an "association" but appointed the petitioners trustees of a "trust" within the meaning of Section 219 of said Revenue Acts of 1921 and 1924, the net income of which should be determined and the tax computed as prescribed in Part I of said Revenue Acts. The petitioners specifically assign error in the determination of net income based on the action of the said Commissioner in including therein the amount distributed by the petitioners to beneficiaries of the Trust.

(b) The Commissioner of Internal Revenue erroneously determined that all sales made by the petitioners during the years 1921, 1922, and 1923 were on the basis of installment sales, whereas certain sales were for cash and were not on [4] the installment plan within the meaning of Section 212(d) of the Revenue Act of 1926 and no part f the collections made on such sales should be included in income for the years 1924 to 1926, inclusive.

(c) In his determination of the percentage of profit on the sale of real estate on installment contracts the Commissioner of Internal Revenue erroneously failed to consider commissions paid to selling agents and other selling expenses. The said Commissioner determined that such commissions and expenses paid in 1921, 1922 and 1923 were ordinary and necessary expenses of doing business for the years in which paid, whereas such commissions and expenses were not ordinary and necessary expenses of doing business for such years but are to be deducted from gross sales price in determining the net profit realized and to be used as the basis for determining the percentage of profit.

(d) In addition to the above assignments of error and as an independent and affirmative allegation, the petitioners allege that the said declaration of trust in so far as it provides that income shall be held and accumulated is in contravention of the laws of the State of California, and that the law required the petitioners to make immediate distribution of all income received and they should have filed fiduciary returns only on behalf of the Trust and not returns of income. The petitioners are therefore not subject to tax but are merely required to file an information return disclosing the amounts distributed to and taxable to the beneficiaries.

5. The facts upon which the petitioners rely as the basis [5] of their proceedings are as follows:

(a) On October 4, 1921, T. A. Morrissey and James M. O'Brien executed a Declaration of Trust

as to certain real estate in the city of Los Angeles. In the Declaration of Trust the said Morrissey and O'Brien declared themselves trustees to collect, hold and distribute the net income of the Trust for the benefit of the beneficiaries whose beneficial interests are represented by certificates of shares. The petitioners filed returns for the Trust as required by Section 219 of the Revenue Acts of 1924 and 1926 and determined the tax as prescribed in Part I of said Acts. The Commissioner of Internal Revenue determined that the Declaration of Trust created an association within the meaning of Section 2 of the said Acts and determined the income and computed the tax as those of a corporation are to be determined and computed under Part II of said Acts.

The declaration of trust recites that certain property had been conveyed to the trustees. This property consisted of 155 acres of land. During the years of 1921 and 1922 the trustees sold beneficial interests in the trust. About 42 acres were surveyed into lots and the sale thereof was begun December 20, 1921 through a broker and his salesmen. The subdivided property was improved by the construction of streets, walks, and curbs during the year 1922. All collections of installments on sales contracts were made through the collection department of a bank. On that part of the property not subdivided a golf course was constructed and completed in September 1922 and a club house in connection therewith was completed in December 1922, which were used by members of the club and their

guests until January 12, 1924. [6] Each beneficiary in the trust received a free membership entitling him to club privileges on payment of the regular fees, and later a few memberships without beneficial interests were sold under a plan requiring refund (less a small monthly amortization, the equivalent of dues) in case of discontinuance of the club activities, which net refunds were paid a short time after the club activities ceased. The club was private and privileges were available only to members and their guests and not to the public generally. No dues were charged, but all persons using the golf course were required to pay a fixed greens fee. The dining room and golf supplies department were operated by concessionaires on a percentage basis. In 1923 a subsidiary corporation was formed and took title to the 113 acres which had not been subdivided and gave back a lease thereon. In November 1923 the property was sold and possession was surrendered on January 12, 1924, at which time it was invested in liquid form to enable quick liquidation and to provide dividends pending dissolution, which would have taken place immediately had it not been for the necessity for the sale of the repurchased improvements and for this tax proceeding. No other activities of any kind were at any time engaged in by the petitioners nor by anyone else on behalf of the Trust.

During the years 1924, 1925 and 1926, and pursuant to the terms of the Declaration of Trust, the petitioners made distributions to the beneficiaries in the respective amounts of $856,828.77, $820,-

648.00 and $817,511.10 on which the [7] beneficiaries paid income tax. These amounts were deducted from income by the petitioners on the returns filed pursuant to said Section 219. The Commissioner of Internal Revenue, having treated the Trust as a corporation, considered the amounts distributed the equivalent of the payment of dividends and denied the same as deductions from income.

(b) The Commissioner of Internal Revenue determined that all sales made during the years 1921, 1922, and 1923 were installment sales within the meaning of Section 212(d) of the Revenue Act of 1926, and included in income for the years 1924, 1925 and 1926 a percentage of profit on collections on such sales. Certain sales made during the years 1921, 1922 and 1923 respectively, the gross sales prices of which were $1,850, $82,705, and $2,125 were not on the basis of installments as defined in said Section 212(d) but were for cash.

(c) During the years 1921, 1922 and 1923 the petitioners paid the sums of $7,272.40, $34,876.09 and $416.05 respectively, representing the commissions of agents and other expenses in connection with the sales of real estate. The Commissioner of Internal Revenue considered these expenditures ordinary and necessary expenses of doing business an deducted the amounts thereof from income for each of the said years and as the result of this he determined that the percentage of profit on sales for the years, 1921, 1922 and 1923 was 50.405%. The percentage determined on the basis of treating the commissions and selling expenses as reductions

to sales price is 35.593% of gross sales. This percentage is determined on the basis of the following: [8]

Gross Sales	$287,365.00	
Less Commissions etc.	42,564.54	
Net Sales Price		$244,800.45
Cost of Land	$100,968.61	
Cost of Improvements	41,549.09	
Total Cost		$142,517.70
Net Profit		$102,282.76

WHEREFORE, petitioners pray that this Board may hear the proceeding, consider the assignments of error and redetermine the tax liability in accordance therewith, and grant such other and further relief as the facts and premises justify.

(s) THEODORE B. BENSON,
917 Southern Building,
Washington, D. C.,
Counsel for Petitioners. [9]

State of California
County of Los Angeles—ss.

James M. O'Brien, being duly sworn, says that he is one of the trustees of the Western Avenue Golf Club appointed under the Declaration of Trust referred to in the foregoing petition, and as such is duly authorized to verify the foregoing petition; that he has read the said petition, or had the same read to him, and is familiar with the statements therein contained, and that the facts therein stated are true except such facts as are stated to be upon

information and belief, and those facts he believes to be true.

(Sgd.) JAMES M. O'BRIEN

Sworn to before me this 3rd day of October, 1928.

THEDA S. BRADLEY

Notary Public [10]

State of California
County of Los Angeles—ss.

T. A. Morrissey, being duly sworn, says that he is one of the trustees of the Western Avenue Golf Club appointed under the Declaration of Trust referred to in the foregoing petition, and as such is duly authorized to verify the foregoing petition; that he has read the said petition, or had the same read to him, and is familiar with the statements therein contained, and that the facts therein stated are true except such facts as are stated to be upon information and belief, and those facts he believes to be true.

Sgd. T. A. MORRISSEY

Sworn to before me this 3rd day of October, 1928.

THEDA S. BRADLEY

Notary Public [11]

EXHIBIT "A"

TREASURY DEPARTMENT
Washington

August 20, 1928

IT:AR:A-5
NMP
Western Avenue Golf Club Trust,
824 Van Nuys Building,
210 West 7th Street,
Los Angeles, California.

Sirs:

In accordance with the provisions of Section 279(a) of the Revenue Act of 1926, there has been assessed against you an income and profits tax amounting to $8,518.12 for the taxable year 1924, 1925 and 1926, the details of which are set forth in the attached statement.

In accordance with the provisions of Section 274(a) of the same Act, you are allowed sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter within which to file a petition with the United States Board of Tax Appeals, contesting in whole or in part the correctness of this determination.

Respectfully,

D. H. BLAIR,
Commissioner.
By C. B. Allen
Deputy Commissioner

Enclosure: Statement Form 882 [12]

STATEMENT

August 20, 1928.

IT:AR:A-5
NMP

In re: Western Avenue Golf Club Trust, 824 Van Nuys Building, 210 West 7th Street, Los Angeles, California.

Years	Deficiency in Tax
1924	$3,567.16
1925	3,240.91
1926	1,710.05
Total	$8,518.12

1924

Net income reported on return		$21,114.30
Add:		
1. Dividends	$56,829.77	
2. Additional profit on real estate sales	6,226.43	63,056.20
		$84,170.50
Deduct:		
3. Dividends, domestic corporations	$53,560.65	
4. Depreciation	26.78	53,587.43
Net income as adjusted		$30,583.07

Explanation of Changes

1. Dividends are held to be a distribution of profits, therefore, are not allowable deductions as

ordinary and necessary business expenses under Section 234 (a) (1), Revenue Act of 1924. [13]

2. Collections in 1924 on real estate sold in 1921 $47,223.57
Per cent profit 50.405%
Realized profit ($47,223.57 x 50.405%) $23,803.04
Realized profit reported 17,576.61
Additional profit $ 6,226.43
Article 45, Regulations 65.

3. Dividends received from domestic corporations are allowable deductions from gross income. Section 234(a)(b) of the Revenue Act of 1924.

4. Depreciation has been allowed in accordance with the provisions of Article 161, Regulations 65. See attached schedule.

Computation of Tax

Net income as adjusted subject to tax at 12½%	$30,583.07
Income tax at 12½%	$ 3,822.88
Tax previously assessed	255.72
Deficiency in tax	$ 3,567.16

1925

Net income reported on return		$23,438.22
Add:		
1. Dividends	$20,648.00	
2. Additional profit on real estate sales	6,243.61	26,891.61
		$50,329.83

Deduct:		
3. Dividends, domestic corporations	$21,973.60	
4. Improvements on land previously sold	261.32	
5. Depreciation	39.47	22,274.39
Net income as adjusted		$28,055.44

[14]

Explanation of Changes.

1. See Explanation #1 for 1924 above. (Section 234(a)(1), Revenue Act of 1926).

2. Collections in 1925 on real estate sold in 1921 $47,032.90

Per cent profit 50.405%

Realized profit ($47,032.90 x 50.405%)	$23,706.93
Realized profit reported	17,463.32
Additional profit	$ 6,243.61

Article 45, Regulations 69.

3. See Explanation #3 for 1924 above. (Section 234(a)(6), Revenue Act of 1926.)

4. This item represents amount expended for improvements on land previously sold which was erroneously included in income reported on return.

5. See attached schedule. (Article 161, Regulations 69).

Computation of Tax

Net income as adjusted subject to tax at 13%		$28,055.44
Income tax at 13%		$ 3,647.28
Tax previously assessed		406.29
Deficiency in tax		$ 3,240.91

1926

Net income reported on return		$16,281.42
Add:		
1. Dividends	$17,511.10	
2. Additional profits on real estate sales	3,539.32	21,050.42
		$37,331.84
Deduct:		
3. Dividends, domestic corporations	$21,973.60	
4. Depreciation	50.08	22,023.68
Net income as adjusted		$15,308.16

[15]

Explanation of Changes.

1. See Explanation #1 for 1924. (Section 234(a)(1), Revenue Act of 1926.)

2. Collections in 1926 on real estate sold in 1921 $25,860.57
   Per cent profit 50.405%
   Realized profit ($25,860.57 x 50.405%) $13,035.02
   Realized profit reported 9,495.70
   Additional profit $ 3,539.32

3. See Explanation #3 for 1924 above. (Section 234 (a)(6), Revenue Act of 1926.)

4. See attached schedule. (Article 161, Regulations 69.)

Computation of Tax

Net income as adjusted	$15,308.16
Less: Exemption	2,000.00
Balance taxable at 13½%	$13,308.16
Income tax at 13½%	$ 1,796.60
Tax previously assessed	86.55
Deficiency in tax	$ 1,710.05

Your claims for refund of $253.72 for 1924, $406.29 for 1925, and $86.55 for 1926 will be rejected. The rejection will officially appear on a schedule to be approved by the Commissioner.

Payment should not be made until a bill is received from the Collector of Internal Revenue for your district, and remittance should then be made to him. [16]

SCHEDULE 1.

Western Avenue Golf Club Trust.

Depreciation Office Furniture

	Balance Purchase	Rate		Reserve December 31, 1923	1924	1925	1926
1924							
January 1	$237.78	10%	12 months	$ 62.16	$ 23.78		
February 29		$11.67	10 months		.97		
April 30		40.66	6 months		2.03		
	$290.11					$ 29.01	
1925							
May 31		$179.25	7 months			10.46	
	$469.36						$ 46.94
1926							
October 31		$131.14	2 months				2.18
November 30		$115.59	1 month				.96
	$716.09						
Totals each year				$ 62.16	$ 26.78	$ 39.47	$ 50.08
Balance to previous period					62.16	88.94	128.41
Amended reserve				$ 62.16	$ 88.94	$128.41	$178.49
Depreciation allowed					$ 26.78	$ 39.47	$ 50.08
Depreciation claimed					None	None	None
Increase					$ 26.78	$ 39.47	$ 50.08

[Title of Court and Cause.]

ANSWER

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the petition herein, admits and denies as follows:

1. Denies the allegations of Paragraph 1 of the petition except the Commissioner admits that T. A. Morrissey and James M. O'Brien are trustees of the Western Avenue Golf Club with the principal place of business at 824 Van Nuys Building, Los Angeles, California.

2. Admits the allegations of Paragraph 2 of the petition.

3. Admits that the taxes in controversy are income taxes for the calendar years 1924 to 1926, inclusive, and are in the amount of $8,518.12.

4. Denies the errors complained of in subparagraphs (a), (b), (c) and (d) of Paragraph 4 of the petition.

5. Denies each and every allegation contained in Paragraph 5 of the petition and its subdivisions which is inconsistent with or contrary to the determination of the Commissioner as set forth in the deficiency letter.

Denies generally and specifically each and every allegation contained in the taxpayer's petition not hereinbefore admitted, qualified or denied.

WHEREFORE, it is prayed that the taxpayer's appeal herein be denied.

(Signed) C. M. CHAREST
General Counsel,
Bureau of Internal Revenue.

Of Counsel:
EARL W. SHINN,
EDWIN M. NIESS,
Special Attorneys,
Bureau of Internal Revenue.

[Endorsed]: United States Board of Tax Appeals. Filed. Nov. 30, 1928 [18]

[Title of Court and Cause.]

MOTION FOR LEAVE TO AMEND PETITION AND AMENDMENTS THERETO

Come now the petitioners by their attorney and move the Board for leave to amend the petition by adding to the assignments of error, under paragraph 4, the following:

(e) That the Commissioner of Internal Revenue erroneously mailed the notice of deficiency addressed to "Western Avenue Golf Club Trust," there being no such legal entity as the said Western Avenue Golf Club Trust and the notice of deficiency does, therefore, not comply with the provisions of Section 274 of the Revenue Act of 1926. [19]

(f) That Section 704 of the Revenue Act of

1928 is not to be construed to apply to this proceeding and if so construed the said section is invalid because in contravention of the provisions of the Constitution of the United States and because in excess of the authority conferred upon Congress by the Constitution.

WHEREFORE the petitioners move to amend their petition, to include the errors above set forth which motion it is understood will not be apposed by counsel for respondent and which amendments it is understood will be answered immediately and it will, therefore, not be necessary to postpone the hearing set for October 23, 1929.

THEODORE B. BENSON,
917 Southern Building,
Washington, D. C.,
Counsel for Petitioner.

[Endorsed]: United States Board of Tax Appeals. Granted Oct. 21, 1929.

[Endorsed]: United States Board of Tax Appeals. Filed Oct. 17, 1929. [20]

[Title of Court and Cause.]

ANSWER TO AMENDMENTS TO PETITION

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the amendment to the petition herein, admits and denies as follows:

(e) Respondent denies the allegation in para-

graph (e) of the amendment to the petition that the notice of deficiency was erroneously mailed to the Western Avenue Golf Club Trust, and further denies the allegation that there was no such legal entity as the Western Avenue Golf Club Trust.

(f) Respondent denies paragraph (f) of the amendment to the petition.

(Signed) C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

Of Counsel:
RALPH S. SCOTT,
EDWIN M. NIESS,
Special Attorneys,
Bureau of Internal Revenue.

[Endorsed]: United States Board of Tax Appeals. Filed Dec. 19, 1929. [21]

[Title of Court and Cause.]

STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto, by their respective attorneys, that the following facts shall be taken as true, provided, however, that this stipulation shall be without prejudice to the right of either party to introduce other and further evidence not inconsistent with the facts herein stipulated to be taken as true.

1. The tax in controversy is that for the calendar years 1923, 1924, 1925, and 1926, but in arriving

at the correct net income for 1923 it is necessary to determine the amount of the net loss if any for the years 1921 and 1922.

2. On October 4, 1921, T. A. Morrissey and James M. O'Brien executed a declaration of trust to certain real estate in the city of Los Angeles, a copy of which said declaration is attached to the Petition in Docket No. 34287 [22] and made a part thereof and marked Exhibit "B". Said Trust was known as Western Avenue Golf Club Trust.

3. The petitioners filed returns as a trust for the years 1921, 1922 and 1923, under the provisions of Section 219 of the Revenue Act of 1921, for the year 1924 under the provisions of Section 219 of the Revenue Act of 1924, and for the years 1925 and 1926 under the provisions of Section 219 of the Revenue Act of 1926, and determined the income and computed the tax as of a trust for all of said years and in the manner prescribed by Part I. of the said Acts. Under date of October 31, 1927, the Commissioner of Internal Revenue made an audit and examination of the above returns of the petitioner and determined that the declaration of trust created an association within the meaning of Part II. of the said Acts and also determined the income and computed the tax as of a corporation.

4. During the years 1921 and 1922 the trustees sold beneficial interests in the trust and paid commissions to salesmen for selling such interests. The beneficial interests were sold at face value and the commissions were paid by the trustees to the salesmen. Payments of such commissions made during

the year 1921 amounted to $5692.90, and during the year 1922 amounted to $5036.15. In the returns made by the trustees for the years 1921 and 1922 the commissions so paid were deducted from gross income in computing the amount of the net loss. In his computations of the net loss for each of the said years the Commissioner of Internal Revenue added the amount of the commissions back to gross income. [23]

5. The property described in the said declaration of trust consisted of 155 acres of land, about 42 acres of which were surveyed into lots and the sale thereof was begun December 20, 1921 through a broker and his salesmen.

6. The commissions to the broker and other selling expenses paid during the year 1921 amounted to $7272.40, during the year 1922 to $34,876.09 and during the year 1923 to $416.05. In the returns filed for the years 1921, 1922 and 1923 the amounts paid as selling expenses were added to the cost of the land in determining the percentage of profit realized on sales made during such years and in determining the percentage of profit on collections made during subsequent years. The respondent determined the amounts paid as commissions and other selling expenses to be deductible expenses for each of the years in which paid and proceeded to determine the net loss for the year 1921 by deducting from gross income the sum of $7272.40, for the year 1922 by deducting from gross income the sum of $34,876.09, and to determine net income for the year 1923 by deducting from gross income the sum of

$416.05, and then proceeded to determine the percentage of profit on sales by eliminating the said amounts from the cost of the land.

7. In his determination of the amount of the net loss for the calendar years 1921 and 1922, and in his determination of the net income for the calendar years 1923, 1924, 1925 and 1926 the respondent treated all sales of lots com- [24] prised in the said 42 acres of land as having been made on the installment basis. Included in the sales determined by the respondent to have been made on the installment basis for the year 1921 were sales in the amount of $1850.00 in which more than 25% of the sales price was received in cash during the said year 1921; included in the sales for the year 1922 were sales in the amount of $82,705.00 in which more than 25% of the sales price was received in cash during the said year 1922; and included in sales for the year 1923 were sales in the amount of $2125.00 in which the cash payment received during the said year was more than 25% of the sales price. It is stipulated that said sales of $1,850.00 in 1921, $82,705.00 in 1922 and $2,125.00 in 1923 shall be treated as cash transactions of 1921, 1922 and 1923, respectively, and that no part of the collections made on said sales during years subsequent to the years in which such cash transactions severally were made shall be treated as taxable income of petitioner for such subsequent years.

8. During the years 1921, 1922, 1923, 1924, 1925 and 1926 the trustees made distributions of profits

to the beneficiaries of the trust in the respective amounts of $138.82, $5662.90, $13,842.22, $56,829.77, $20,648.00 and $17,511.10. In the returns filed for the said years the amounts so distributed were deducted from gross income. The respondent, having determined as aforesaid that the declaration of trust created an association, denied the said deductions and restored the said amounts to gross income [25] for the purpose of determining the amount of the net loss for the years 1921 and 1922, and the net income for the years 1923, 1924, 1925 and 1926.

9. The 42 acres of land abovementioned were surveyed and platted into lots and beginning December 20, 1921, the lots were sold through a broker and his salesmen. The subdivided property was during the year 1922 improved by the construction of streets, side-walks and curbs. All of the lots were sold during 1921, 1922 and 1923 and collections on sales contracts were made through the collection department of a bank.

10. On that part of the property not subdivided a golf course was constructed, and completed in September 1922 and a club house connected with it was completed in December 1922, which were used by the members of the club and their guests until January 12, 1924 on which date all club activities ceased. Each beneficiary in the trust received a free membership entitling him to club privileges on the payment of the regular fees and later memberships without beneficial interests were sold under a plan requiring refund (less a small monthly amortization, the equivalent of dues) in case of discontinu-

ance of the club activities, which net refunds were in fact paid a short time after the club activities ceased on the date hereinabove mentioned. The club was private and privileges were available only to members and their guests and not to the public in general. No dues were charged, but all persons using the golf course [26] were required to pay a fixed greens fee. The dining room and golf supplies department were operated by concessionaires on a percentage basis.

11. In July, 1923, the 113 acres of land comprising the golf course, together with all improvements and equipment, were conveyed and transferred to Western Avenue Golf Club, Inc., a California Corporation, in exchange for its stock, and without other consideration. No tax on said transfer was paid by petitioners and none is claimed by respondent to be payable thereon. During the years 1924, 1925, and 1926 petitioner received from said corporation dividends upon the Stock thereof so acquired by the petitioner amounting in 1924 to $53,560.65, in 1925 to $21,973.60 and in 1926 to $21,973.60, all of which were returned as income by petitioner for the years in which they were received. Respondent in his determination of the tax liability of petitioner, eliminated said dividends from the taxable income of petitioner for the years in which such dividends were so received, treating such dividends as non-taxable against petitioner, as an association.

12. Petitioner, under a lease from said Western Avenue Golf Club, Inc., continued the operation of

said golf course until January 12, 1924 on which date such operations ceased. The gross receipts from said golf course operations during said 12 day period in 1924 amounted to less than $400.00 which amount was included by petitioner in gross income returned. [27]

13. The installation of and payment for improvements in said 42 acre subdivision was begun in 1921 and finished in 1922. Sales of lots in said subdivision were begun in 1921 and finished in 1922. Collections of installments of principal and interest upon the contracts of purchase of lots in said subdivision were made in 1921 to 1926 inclusive, by a bank as collection agent for petitioner. Petitioner also during said years collected certain assignment fees from purchasers upon the assignment by them of their contracts of purchase. During the period from September 1, 1922 until January 12, 1924 petitioner collected, (1) from members and their guests certain fees for the use of said golf course, (2) from members certain assignment fees upon the assignment of their memberships, and (3) from concessionaires operating such club departments as dining room, golf shop, etc., certain rents for such concessions. No activities have been engaged in by petitioner between December 31, 1923 and January 1, 1927 except (1) operation of said golf course for the first 12 days of 1924 as aforesaid, (2) Receipt from collection agent bank of principal and interest so collected by said bank in behalf of petitioner, (3) Receipt of credit of interest earned on bank balances, (4) Receipt of assignment fees in

assignment of lot purchase contracts by holders thereof, (5) Conveyance of lots to purchasers thereof, (6) Receipt of dividends from Western Avenue Golf Club, Inc., upon shares thereof owned by petitioner, (7) Distribution of moneys [28] to holders of beneficial interests in petitioner trust by way of dividends and, in some cases, by way of redemption and retirement of their beneficial interests.

14. T. A. Morrissey and J. M. O'Brien, who were appointed as sole trustees of petitioner Western Avenue Golf Club Trust by the aforementioned declaration of Trust have ever since continued to be and now are the sole trustees of said petitioner. The number of beneficial interests issued by said petitioner Western Avenue Golf Club Trust and outstanding between December 31, 1922 and January 1, 1927, and the number of said beneficial interests owned during said period by said named trustees as individuals were as follows:

Column 1 Date	Column 2 Total No. Outstanding	Column 3 Total No. owned by T. A. Morrissey	Column 4 Total No. owned by J. M. O'Brien	Column 5 Total of Columns 3 & 4	Column 6 Percentage Ratio of Column 5 to Column 2
Dec. 31, 1922	3019	169 24/100	1107 69/100	1276 93/100	42.3%
Mar. 31, 1923	3013	"	"	"	42.4%
June 30, 1923	"	"	"	"	"
Sept. 30, 1923	3015	"	"	"	"
Dec. 31, 1923	3016	110	375 22/100	485 22/100	16. %
Mar. 31, 1924	2897	83	"	451 22/100	15.8%
June 30, 1924	2783	"	412 22/100	495 22/100	17.7%
Sept. 30, 1924	2712	"	"	"	18.2%
Dec. 31, 1924	2680	"	"	"	18.4%
Mar. 31, 1925	2607	133	416 91/100	594 91/100	22.8%
June 30, 1925	2596	"	"	"	22.9%
Sept. 30, 1925	2570	"	"	"	23.1%
Dec. 31, 1925	2561	170 93/100	"	632 84/100	24.7%
Mar. 31, 1926	2407	"	"	"	26.2%
June 30, 1926	2203	"	"	"	28.7%
Sept. 30, 1926	2175	"	"	"	29 %
Dec. 31, 1926	2172	"	"	"	29.1%

[29]

The number of benefical interests owned by said trustees as individuals did not at any time during said period exceed the number shown above nor exceed the percentage shown above of the whole number then outstanding.

The following is the approximate number of persons holding beneficial interests in said Western Avenue Golf Club Trust on the dates shown, to wit:

Dec. 31, 1922	890	Persons
" " 1923	920	"
" " 1924	675	"
" " 1925	570	"
" " 1926	275	"

Done this 9th day of June, 1932.

THEODORE B. BENSON
JAMES M. O'BRIEN
Attorneys for Petitioner.
C. M. CHAREST, J.M.L.,
Attorney for Respondent.

[Endorsed]: United States Board of Tax Appeals. Filed at hearing June 10, 1932. Div. 5, Docket Nos. 34287, 40977. [30]

[Title of Court and Cause.]

Docket Nos. 34287, 40977.

James M. O'Brien, Esq., and Theodore B. Benson, Esq., for the petitioners.
J. M. Leinenkugel, Esq., for the respondent.

MEMORANDUM OPINION.

SMITH: These proceedings, consolidated for hearing, are for the redetermination of deficiencies in income tax for 1923 (Docket No. 34287), 1924, 1925, and 1926 (Docket No. 40977), in the respective

amounts of $1,889.70, $3,567.16, $3,240.91, and $1,710.05. Some of the allegations of error contained in the petition have been waived and another has been [31] settled by stipulation of facts. The petitioners appealing to this Board on behalf of Western Avenue Golf Club are hereinafter referred to as the petitioner. The issues to be determined are:

1. Whether the deficiency notices herein were sent to the petitioner in accordance with the provisions of section 274 of the Revenue Act of 1926.

2. Whether section 704 of the Revenue Act of 1928 is unconstitutional if construed to apply to these proceedings.

3. Whether the petitioner is taxable as a trust or as an association in the years 1921 to 1926, inclusive.

4. Whether all sales of real estate made by the petitioner in 1921, 1922, and 1923 were on the installment basis or whether some of the sales were for cash.

5. Whether in computing the profits realized by the petitioner on installment sales of real estate in 1921, 1922, and 1923 the commissions paid to agents and other selling expenses are deductible from gross income in those years, or whether they are deductible from the sales prices in determining the percentage of profits on the installment sales.

6. Whether the commissions paid by the petitioner in 1921 and 1922 on the sales of its certificates of shares to the beneficiaries are deductible as ordinary and necessary expenses of those years.

7. Whether the petitioner is taxable upon any of its income in the years involved in these proceed-

ings in view of the fact, as alleged, that under the laws of the State of California, it was prohibited from accumulating any of its income for the beneficiaries. [32]

The years 1921 and 1922 are in issue only for the purpose of determining the net losses, if any, for those years which are deductible from the gross income of 1923. The parties have filed a written stipulation setting forth the principal facts.

The petitioner was created by a declaration of trust executed on October 4, 1921, by T. A. Morrissey and James M. O'Brien, who were therein designated trustees and who, in their "collective capacity," were to be known as "Western Avenue Golf Club." Under the provisions of the instrument, Morrissey and O'Brien were to hold certain real estate, comprising a tract of 155 acres, situated in the City of Los Angeles, California—

> "* * * which property has already been conveyed to us, and also any and all other property, real, personal, or mixed, which may hereafter be conveyed or transferred to or acquired by us or them [their successors] as trustees hereunder, together with the proceeds and avails thereof in trust upon the trusts hereinafter set forth to maintain and to dispose of the same, and to collect, receive, hold and distribute the net income thereof for the benefit of the beneficiaries from time to time, whose beneficial interests in said property are represented by certificates for shares of beneficial interest issued hereunder according to the num-

ber of such shares held by them respectively, and in accordance with the priorities hereinafter expressed, and in the manner and subject to the stipulation herein contained, * * *"

The instrument further provides that—

"18. During the continuance of this trust the beneficial interests therein and thereunder shall be solely evidenced by certificates for shares of beneficial interest for which provision is hereinafter made.

"19. Such beneficial shares shall be divided into two thousand (2,000) preferred shares of the par value of One Hundred ($100.00) Dollars each, and two thousand (2,000) common shares of no par value." [33]

The holders of the preferred shares were entitled to receive $8 per share per annum out of the "surplus profits" or "surplus dividends." The holders of the common shares were entitled to receive—

"* * * when and as declared by the trustees out of the surplus profits arising from the business of said trust, or surplus, dividends at such rate as may be determined and decided upon by the trustees in the exercise of their absolute discretion, not exceeding the rate of $8.00 per share per annum, * * *"

The remaining profits, if any, were to be distributed at the discretion of the trustees to both the preferred and common shareholders.

The trustees were authorized to make additional assessments against the common shares in the same

manner as provided by the Civil Code of California in the case of corporations organized for profit, with certain exceptions not here material.

The trustees had exclusive management of and control over the business and property of the trust—

> "* * * it being expressly declared that the said shareholders, otherwise sometimes referred to herein as beneficiaries, are cestuis que trustent, and hold no other relation to the trustees than that of cestuis que trustent hereunder. The shareholders shall only have the rights specifically set forth in this instrument, that is to say, the right to dividends, only as the same shall be declared by the trustees, * * *"

The trustees were empowered to increase their own number and to elect successor trustees by a majority vote. They were also authorized to appoint an advisory board to be known as directors, consisting of not more than 15 persons but the appointment of such board was not in any way to limit their own powers.

The written stipulation of facts referred to above is in part as follows: [34]

> "3. The petitioners filed returns as a trust for the years 1921, 1922 and 1923, under the provisions of Section 219 of the Revenue Act of 1921, for the year 1924 under the provisions of Section 219 of the Revenue Act of 1924, and for the years 1925 and 1926 under the provisions of Section 219 of the Revenue Act of

1926, and determined the income and computed the tax as of a trust for all of said years and in the manner prescribed by Part I. of the said Acts. Under date of October 31, 1927, the Commissioner of Internal Revenue made an audit and examination of the above returns of the petitioner and determined that the declaration of trust created an association within the meaning of Part II. of the said Acts and also determined the income and computed the tax as of a corporation.

"4. During the years 1921 and 1922 the trustees sold beneficial interests in the trust and paid commissions to salesmen for selling such interests. The beneficial interests were sold at face value and the commissions were paid by the trustees to the salesmen. Payments of such commissions made during the year 1921 amounted to $5692.90, and during the year 1922 amounted to $5036.15. In the returns made by the trustees for the years 1921 and 1922 the commissions so paid were deducted from gross income in computing the amount of the net loss. In his computations of the net loss for each of the said years the Commissioner of Internal Revenue added the amount of the commissions back to gross income.

"5. The property described in the said declaration of trust consisted of 155 acres of land, about 42 acres of which were surveyed into lots and the sale thereof was begun December 20, 1921 through a broker and his salesmen.

"6. The commissions to the broker and other selling expenses paid during the year 1921 amounted to $7272.40, during the year 1922 to $34,876.09 and during the year 1923 to $416.05. In the returns filed for the years 1921, 1922 and 1923 the amounts paid as selling expenses were added to the cost of the land in determining the percentage of profit realized on sales made during such years and in determining the percentage of profit on collections made during subsequent years. The respondent determined the amounts paid as commissions and other selling expenses to be deductible expenses for each of the years in which paid and proceeded to determine the net loss for the year 1921 by deducting from gross income the sum of $7272.40, for the year 1922 by deducting from gross income the sum of $34,876.09, and to determine net income for the year 1923 by [35] deducting from gross income the sum of $416.05, and then proceeded to determine the percentage of profit on sales by eliminating the said amounts from the cost of the land.

"7. In his determination of the amount of the net loss for the calendar years 1921 and 1922, and in his determination of the net income for the calendar years 1923, 1924, 1925 and 1926 the respondent treated all sales of lots comprised in the said 42 acres of land as having been made on the installment basis. Included in the sales determined by the respondent to have been made on the installment

basis for the year 1921 were sales in the amount of $1850.00 in which more than 25% of the sales price was received in cash during the said year 1921; included in the sales for the year 1922 were sales in the amount of $82,705.00 in which more than 25% of the sales price was received in cash during the said year 1922; and included in sales for the year 1923 were sales in the amount of $2,125.00 in which the cash payment received during the said year was more than 25% of the sales price. It is stipulated that said sales of $1,850.00 in 1921, $82,705.00 in 1922 and $2,125.00 in 1923 shall be treated as cash transactions of 1921, 1922 and 1923, respectively, and that no part of the collections made on said sales during years subsequent to the years in which such cash transactions severally were made shall be treated as taxable income of petitioner for such subsequent years.

"8. During the years 1921, 1922, 1923, 1924, 1925 and 1926 the trustees made distributions of profits to the beneficiaries of the trust in the respective amounts of $138.82, $5662.90, $13,842.22, $56,829.77, $20,648.00 and $17,511.10. In the returns filed for the said years the amounts so distributed were deducted from gross income. The respondent, having determined as aforesaid that the declaration of trust created an association, denied the said deductions and restored the said amounts to gross income for the purpose of determining the amount of the net loss for the years 1921 and 1922, and the net income for the years 1923, 1924, 1925 and 1926.

"9. The 42 acres of land abovementioned were surveyed and platted into lots and beginning December 20, 1921, the lots were sold through a broker and his salesmen. The subdivided property was during the year 1922 improved by the construction of streets, sidewalks and curbs. All of the lots were sold during 1921, 1922 and 1923 and collections on sales contracts were made through the collection department of a bank. [36]

"10. On that part of the property not subdivided a golf course was constructed and completed in September 1922 and a club house connected with it was completed in December 1922, which were used by the members of the club and their guests until January 12, 1924 on which date all club activities ceased. Each beneficiary in the trust received a free membership entitling him to club privileges on the payment of the regular fees and later memberships without beneficial interests were sold under a plan requiring refund (less a small monthly amortization, the equivalent of dues) in case of discontinuance of the club activities, which net refunds were in fact paid a short time after the club activities ceased on the date hereinabove mentioned. The club was private and privileges were available only to members and their guests and not to the public in general. No dues were charged, but all persons using the golf course were required to pay a fixed greens fee. The dining room and golf

supplies department were operated by concessionaires on a percentage basis.

"11. In July 1923, the 113 acres of land comprising the golf course, together with all improvements and equipment, were conveyed and transferred to Western Avenue Golf Club, Inc., a California Corporation, in exchange for its stock, and without other consideration. No tax on said transfer was paid by petitioners and none is claimed by respondent to be payable thereon. During the years 1924, 1925, and 1926 petitioner received from said corporation dividends upon the Stock thereof so acquired by the petitioner amounting in 1924 to $53,560.65, in 1925 to $21,973.60 and in 1926 to $21,973.60, all of which were returned as income by petitioner for the years in which they were received. Respondent in his determination of the tax liability of petitioner, eliminated said dividends from the taxable income of petitioner for the years in which such dividends were so received, treating such dividends as non-taxable against petitioner, as an association.

"12. Petitioner, under a lease from said Western Avenue Golf Club, Inc., continued the operation of said golf course until January 12, 1924 on which date such operations ceased. The gross receipts from said golf course operations during said 12 day period in 1924 amounted to less than $400.00 which amount was included by petitioner in gross income returned.

"13. The installation of and payment for improvements in said 42 acre subdivision was begun in 1921 and finished in 1922. Sales of lots in said subdivision were begun in 1921 and finished in 1922. Collections of installments of principal and [37] interest upon the contracts of purchase of lots in said subdivision were made in 1921 to 1926 inclusive, by a bank as collection agent for petitioner. Petitioner also during said years collected certain assignment fees from purchasers upon the assignment by them of their contracts of purchase. During the period from September 1, 1922 until January 12, 1924 petitioner collected, (1) from members and their guests certain fees for the use of said golf course, (2) from members certain assignment fees upon the assignment of their memberships, and (3) from concessionaires operating such club departments as dining room, golf shop, etc., certain rents for such concessions. No activities have been engaged in by petitioner between December 31, 1923 and January 1, 1927 except: (1) operation of said golf course for the first 12 days of 1924 as aforesaid, (2) Receipt from collection agent bank of principal and interest so collected by said bank in behalf of petitioner, (3) Receipt of credit of interest earned on bank balances, (4) Receipt of assignment fees in assignment of lot purchase contracts by holders thereof, (5) Conveyance of lots to purchasers thereof, (6) Receipt of dividends from Western Avenue Golf Club, Inc., upon shares thereof owned

by petitioner, (7) Distribution of moneys to holders of beneficial interests in petitioner trust by way of dividends and, in some cases, by way of redemption and retirement of their beneficial interests.

"14. T. A. Morrissey and J. M. O'Brien, who were appointed as sole trustees of petitioner Western Avenue Golf Club Trust by the aforementioned declaration of Trust have ever since continued to be and now are the sole trustees of said petitioner. The number of beneficial interests issued by said petitioner Western Avenue Golf Club Trust and outstanding between December 31, 1922 and January 1, 1927, and the number of said beneficial interests owned during said period by said named trustees as individuals were as follows: [38]

Column 1 Date	Column 2 Total No. Outstanding	Column 3 Total No. owned by T. A. Morrissey	Column 4 Total No. owned by J. M. O'Brien	Column 5 Total of Columns 3 & 4	Column 6 Percentage Ratio of Column 5 to Column 2
Dec. 31, 1922	3019	169 24/100	1107 69/100	1276 93/100	42.3%
Mar. 31, 1923	3013	"	"	"	42.4%
June 30, 1923	"	"	"	"	"
Sept. 30, 1923	3015	"	"	"	"
Dec. 31, 1923	3016	110	375 22/100	485 22/100	16. %
Mar. 31, 1924	2897	83	"	451 22/100	15.8%
June 30, 1924	2783	"	412 22/100	495 22/100	17.7%
Sept. 30, 1924	2712	"	"	"	18.2%
Dec. 31, 1924	2680	"	"	"	18.4%
Mar. 31, 1925	2607	133	416 91/100	594 91/100	22.8%
June 30, 1925	2596	"	"	"	22.9%
Sept. 30, 1925	2570	"	"	"	23.1%
Dec. 31, 1925	2561	170 93/100	"	632 84/100	24.7%
Mar. 31, 1926	2407	"	"	"	26.2%
June 30, 1926	2203	"	"	"	28.7%
Sept. 30, 1926	2175	"	"	"	29 %
Dec. 31, 1926	2172	"	"	"	29.1%

The number of benefical interests owned by said trustees as individuals did not at any time during said period exceed the number shown above nor exceed the percentage shown above of the whole number then outstanding.

The following is the approximate number of persons holding beneficial interests in said Western Avenue Golf Club Trust on the dates shown, to wit:

Dec. 31, 1922	890	Persons
" " 1923	920	"
" " 1924	675	"
" " 1925	570	"
" " 1926	275	"

The issues will be discussed in the order in which they appear above. [39]

1. and 2. The petitioner's first and second contentions are that there is and was no such legal entity as the Western Avenue Golf Club or the Western Avenue Golf Club Trust and that the notices of deficiency upon which the petitions to the Board are predicated do not comply with the provisions of section 274 of the Revenue Act of 1926, and that section 704 of the Revenue Act of 1928 is not to be construed to apply to these proceedings, and that if so construed it is invalid because in contravention of the provisions of the Constitution of the United States and because in excess of the authority conferred upon Congress by the Constitution.

The deficiency notice in Docket No. 34287, for 1923, was addressed to "Western Avenue Golf Club, T. A. Morrissey and J. M. O'Brien, Trustees," and in Docket No. 40977, the deficiency notice for 1924, 1925, and 1926 was addressed to "Western Avenue Golf Club Trust," both notices being addressed to 824 Van Nuys Building, Los Angeles, California, the

petitioner's correct address. The petitions in both docket numbers were filed in the name of "T. A. Morrissey and James M. O'Brien, Trustees of an Express Trust, known as Western Avenue Golf Club." Apparently the deficiencies set forth in the deficiency notices referred to were computed from the returns filed by Western Avenue Golf Club as a trust.

Clearly, the trustees were the proper parties to file the petitions with the Board. Cf. William B. Thalhimer, et al., Executors, v. Commissioner, 62 Fed. (2d) 703, (C. C. A. 4), decided January 10, 1933. The petitioner has not advanced any valid reason why section 704 should be held unconstitutional as applied to these proceedings. [40]

We can see no merit in either of these contentions. They are not argued by the petitioner in its brief and we can find no support for them either in the facts or in the law.

3. The substance of this contention is that the petitioner was not an association taxable as a corporation in the years 1921 to 1926, inclusive, but was a trust taxable under section 219 of the Revenue Acts of 1921, 1924, and 1926.

Section 704 of the Revenue Act of 1928 provides in part that—

> "(a) If a taxpayer filed a return as a trust for any taxable year prior to the taxable year 1925 such taxpayer shall be taxable as a trust for such year and not as a corporation, if such taxpayer was considered to be taxable as a trust

and not as a corporation either (1) under the regulations in force at the time the return was made or at the time of the termination of its existence, or (2) under any ruling of the Commissioner or any duly authorized officer of the Bureau of Internal Revenue applicable to any of such years, and interpretative of any provision of the Revenue Act of 1918, 1921, or 1924, which had not been reversed or revoked prior to the time the return was made, or under any such ruling made after the return was filed which had not been reversed or revoked prior to the time of the termination of the taxpayer's existence."

We have heretofore held in applying this section of the Act that under the Commissioner's Regulations and Bureau rulings, in effect up to and including the calendar year 1923, and prior to the change in the Commissioner's rulings giving effect to the decision in Hecht v. Malley, 265 U. S. 144, decided May 12, 1924, the test to be applied in distinguishing trusts from associations was whether the beneficiaries of shareholders controlled the action of the trustees. See E. A. Landreth Co., et al., 15 B. T. A. 655; Van Cleave Trust, 18 B. T. A. 486; [41] Commercial Trust Co., 18 B. T. A. 1248; Rollin S. Sturgeon, et al., Trustees, 25 B. T. A. 368; Twin Bell Oil Syndicate, 26 B. T. A. 165. Under the trust instrument herein considered, the shareholders had no control over the trustees or the management of the business. The trustees filed returns as a trust

for all of the years 1921 to 1926, inclusive. We therefore hold that the petitioner is taxable as a trust for the years 1921, 1922, and 1923. For the subsequent years 1924, 1925, and 1926, the test to be applied, as stated in Rollin S. Sturgeon, et al., Trustees, supra, is whether—

> "* * * (1) the beneficiaries of the alleged trust have voluntarily associated themselves together in the general form and mode of procedure of a corporation, and (2) are organized to, and in fact are, engaged in the active conduct of a business for profit, or (3) whether the trustees are merely holding the property and collecting the income therefrom and distributing to those beneficially interested. Extension Oil Co., 16 B. T. A. 1028; affd., 47 Fed. (2d) 65; Jackson-Wermich Trust, 24 B. T. A. 150; E. B. Galbreath, et al., 24 B. T. A. 1107."

The petitioner was created principally for the purpose of developing and selling the tract of real estate which was conveyed to it by Morrissey and O'Brien, and in conjunction therewith to operate a golf course and other adjuncts of the real estate subdivision. These activities were begun immediately. The petitioner was clearly an active business trust as distinguished from a liquidating trust.

It is apparent, too, from the provisions of the trust instrument, which we will not discuss in detail, that the petitioner had many of the characteristics indicative of corporate organization. We are of the [42] opinion, therefore, that for the

years 1924, 1925, and 1926 the petitioner is taxable as an association. See also Little Fork Oil & Gas Co. v. Lewellyn, 29 Fed. (2d) 137; Trust No. 5833, Security First Nat. Bank of Los Angeles v. Welch, 54 Fed. (2d) 323; Twin Bell Oil Syndicate, supra, and cases therein cited.

The fact that the petitioner did not make any sales of real estate after early in 1923 does not alter its taxable status for the subsequent years during which it continued to receive profits and distribute them to the beneficiaries. G. F. Sloan, et al., v. Commissioner, ... Fed. (2d) ....., (C. C. A. 9), decided February 20, 1933, affirming G. F. Sloan, et al., 24 B. T. A. 61.

4. This issue is settled by the facts stated in paragraph 3 above of the written stipulation.

5. The petitioner contends that the commissions and other expenses of selling the subdivision lots in 1921, 1922, and 1923 should be deducted from the sales prices and thus pro-rated over the installment contracts for the purpose of determining the percentage of profits realized on installment sales rather than deducted from gross income as ordinary and necessary expenses of the years of such sales. The petitioner so treated these items in its returns for 1921, 1922, and 1923 when the sales were made. The petitioner was not a dealer in real estate. It was organized as above stated for the purpose of developing and selling the single tract of land conveyed to it by Morrissey and O'Brien. It never acquired or sold any other real estate. It never held a broker's license. The [43] sales of the lots were

made through a broker. The petitioner's contention on this issue is sustained upon authority of Mrs. E. A. Griffin, 19 B. T. A. 1243, and cases following that decision.

6. The petitioner seeks to deduct as ordinary and necessary expenses commissions paid to salesmen on sales of its own shares in 1921 and 1922 in the amounts of $5,692.90 and $5,036.15, respectively. We are of the opinion that these amounts are not deductible. Such expenditures are of a capital nature and are therefore not deductible as business expenses. They serve to reduce the selling price of the capital stock or shares. Charles H. Lilly Co., 2 B. T. A. 1058; Emerson Electric Mfg. Co., 3 B. T. A. 932; Simmons Co., 8 B. T. A. 631; affd. 33 Fed. (2d) 75; Corning Glass Works, 9 B. T. A. 771; affd. 37 Fed. (2d) 798.

7. With respect to this issue, the petitioner states in its brief that—

> "Because its declaration of trust contained what was then a customary provision in California trusts allowing the trustees to accumulate income, Petitioner trust believed that under the law and regulations it would be required to return and pay the tax, instead of having the beneficiaries do so. However, the Supreme Court of California in the case of Estate of Yates, 170 Calif. 254, [149 Pac. 555], has held that such provisions allowing the accumulation are void. This then squarely places petitioner trust in the classification of trusts whose in-

come must be returned by the beneficiaries and whose tax must be paid by them."

We decided this identical question in Max Wolf, et al., Trustees, 10 B. T. A. 835, where we held that the provision of a trust for the accumulation of income was void under the laws of the State of California and that the income was therefore distributable to the beneficiaries and taxable to them rather than to the trust entity under the provisions of [44] section 219 of the Revenue Acts of 1918 and 1921. Sections 723 and 724 of the Civil Code of California, 1927, Deering, read in part as follows:

"§ 723. Accumulations, when void. All directions for the accumulation of the income of property, except such as are allowed by this title, are void.

* * * * * * *

"§ 724. Accumulation of income. An accumulation of the income of property, for the benefit of one or more persons, may be directed by any will or transfer in writing sufficient to pass the property out of which the fund is to arise, as follows:

1. If such accumulation is directed to commence on the creation of the interest out of which the income is to arise, it must be made for the benefit of one or more minors then in being, and terminate at the expiration of their minority; or,

2. If such accumulation is directed to com-

mence at any time subsequent to the creation of the interest out of which the income is to arise, it must commence within the time in this title permitted for the vesting of future interests, and during the minority of the beneficiaries, and terminate at the expiration of such minority."

For other judicial decisions holding the directions for the accumulation of income void under the laws of the State of California, see in re Pforr's Estate, 144 Cal. 121; 77 Pac. 825; In re Duffill's Estate, 180 Cal. 748; 183 Pac. 337.

We also held in Estate of Henry Mayer, 16 B. T. A. 1164, that the income of a trust, created and existing under the laws of Pennsylvania, which likewise prohibited the accumulation of income, was distributable to the beneficiaries and therefore taxable to them rather than to the trust, under section 219 of the Revenue Acts of 1918 and 1921. Upon authority of the cases cited, we hold that the petitioner's income in the years 1921, 1922, and 1923 was distributable to the beneficiaries and is therefore [45] taxable to them and not to the petitioner. This determination, however, has no application to the subsequent years 1924, 1925, and 1926 for which we have determined that the petitioner was an association taxable as a corporation.

Judgment will be entered under Rule 50.

[Endorsed]: United States Board of Tax Appeals. Entered Mar. 24, 1933. [46]

United States Board of Tax Appeals
Washington

Docket Nos. 34287, 40977.

T. A. MORRISSEY and JAMES M. O'BRIEN, Trustees of an Express Trust, known as WESTERN AVENUE GOLF CLUB,
Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DECISION.

Pursuant to the Memorandum Opinion in the above proceedings, entered March 24, 1933, counsel for the respondent, on May 24, 1933, filed a notice of settlement which was set down for hearing, under Rule 50 of the Board's Rules of Practice, on June 21, 1933. Counsel for the petitioners did not appear at the hearing and have filed no objections to the redetermination of the deficiencies made by the respondent. Upon examination, the Board finds that the redetermination made by the respondent is in accord with the Memorandum Opinion entered March 24, 1933. Wherefore, it is—

ORDERED and DECIDED that there is an overpayment of income tax for 1923 in the amount of $489.29 and overassessments to be abated for the years 1924, 1925, and 1926 of $1,676.61, $1,617.42, and $673.15, respectively; and that there are unpaid portions of the correct tax liability to be collected for the years 1924, 1925, and 1926 of $1,890.55,

$1,623.49, and $1,036.90, respectively.

[Signed] C. M. CHAREST,

[Seal] Member.

[Endorsed]: Entered Jun. 23, 1933. [47]

[Title of Court and Cause.]

To the Honorable the Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

The petitioners, T. A. Morrissey and James M. O'Brien, trustees of an express trust, known as Western Avenue Golf Club, in support of this their petition, filed pursuant to provisions of Section 1001 of the Act of Congress approved February 26, 1926, (44 Stat. 109), entitled the Revenue Act of 1926, and as amended by Section 608 of the Revenue Act of 1928, (45 Stat. 873), and by Section 1101 of the Revenue Act of 1932, (47 Stat. 286), for the review of the decision of the United States Board of Tax Appeals entered June 23, 1933, Docket No. 40977, respectfully shows to this Honorable Court as follows:

I.

DESIGNATION OF THE COURT OF REVIEW.

The petitioners being agrieved by the decision of the [48] Board of Tax Appeals hereinafter described redetermining deficiencies for the calendar years 1924, 1925 and 1926 in the amounts of $1,890.55, $1,623.49, and $1,036.90, and the said T. A. Morrissey and James M. O'Brien being citizens of

the United States and inhabitants of the State of California with postoffice address at 824 I. N. Van Nuys Building, Los Angeles, California, and the returns for each of the said years having been filed with the Collector of Internal Revenue for the Sixth District of California at Los Angeles, California, desire a review of the said decision of the said United States Board of Tax Appeals by the Circuit Court of Appeals for the Ninth Circuit within which Circuit the petitioners reside and within which Circuit is located the office of the said collector of internal revenue.

II.

STATEMENT OF THE NATURE OF THE CONTROVERSY.

1. That on October 11, 1928 the petitioners filed with the United States Board of Tax Appeals their petition for the redetermination of alleged deficiencies in income tax for the years 1924, 1925 and 1926 in the amounts of $3,567.16, $3,240.91 and $1,710.05 as shown by a notice of deficiency previously mailed to the petitioners by the Commissioner of Internal Revenue on August 20, 1928, the allegations of which said petition in so far as are relative to this petition for review are in substance as follows:

That the petitioners, T. A. Morrissey and James M. O'Brien, are trustees of an express trust known as Western Avenue Golf [49] Club with office and principal place of business at 824 I. N. Van Nuys Building, Los Angeles, California; that the Commissioner of Internal Revenue on August 20, 1928

mailed to the petitioner a notice of deficiency showing deficiencies as above stated; that in the said notice of deficiency the Commissioner of Internal Revenue erred in determining that the said declaration of trust created an "association" within the meaning of Section 2 of the Revenue Acts of 1924 and 1926, and as a result thereof the Commissioner determined the net income and computed the tax in the manner and at the rates set forth in Part 2 of the said Revenue Acts, whereas in law and fact the declaration of trust did not create such an "association" but appointed the petitioners trustees of a "trust" within the meaning of Section 219 of the said Revenue Acts of 1921 and 1924, the net income of which should be determined and the tax computed as prescribed in Part 1 of said Revenue Acts; that in addition to the above assignment of error and as an independent and affirmative allegation, the petitioners allege that the said declaration of trust, in so far as it provides that income shall be held and accumulated is in contravention of the laws of the State of California, and that the laws of the said State require the petitioners to make immediate distribution of all income received, and that pursuant to the provisions of the said laws of California the petitioners should have filed fiduciary returns only on behalf of the trust and not on returns of income; and that the said Commissioner of Internal Revenue in his determination of tax for the said years committed certain other errors not [50] here material.

2. That thereafter and on November 30, 1928 the Commissioner of Internal Revenue filed with the said Board his answer to the said petition and therein admitted that the said T. A. Morrissey and James M. O'Brien are trustees of an express trust known as Western Avenue Golf Club with office and principal place of business at 824 I. N. Van Nuys Building, Los Angeles, California; and that the tax in controversy is that for the years 1924, 1925 and 1926 in the respective amounts of $3,567.16, $3,240.91 and $1,710.05; and therein denied that the Commissioner of Internal Revenue committed any error in his determination of the said deficiency.

3. That on October 17, 1929 the petitioners moved to amend the said petition as to matters not here important, which said motion was granted October 21, 1929 and to which the said amended petition the Commissioner of Internal Revenue filed his answer October 21, 1929.

4. The cause being at issue under the rules of practice of the said Board on the filing of the said answer to the original petition and on the filing of the said answer to the amended petition duly came on for hearing before a member of the Board at Los Angeles, California, on June 10, 1932, at which time the parties agreed to a stipulation of facts, and in addition thereto the petitioners by competent witnesses offered testimony in support of the allegations in their petition as aforesaid, and the cause was argued and submitted whereupon the Board on March 24, 1933 rendered its findings of fact and opinion and therein held that the said declara- [51]

tion of trust created an association within the meaning of the said provisions of the said Revenue Acts of 1924 and 1926, and further said that the said declaration of trust did not violate the said laws of California as to accumulation of income. On June 23, 1933 the said Board entered its decision redetermining the deficiency as above stated.

ASSIGNMENT OF ERROR.

1. The said Board erred in entering judgment for the Commissioner of Internal Revenue for each of the said years.

2. The said Board erred in redetermining the said deficiencies for the said years.

3. The said Board erred in holding as a matter of law that the said declaration of trust created an "association" within the meaning of Section 2 of the Revenue Acts of 1924 and 1926, and in determining the net income and computing the tax in the manner and at the rate set forth in Part II of the said Revenue Acts relating to corporations.

4. The said Board erred in not holding that the said declaration of trust created a "trust" within the meaning of Section 219 of the said Revenue Acts of 1924 and 1926, and that the income should be determined and the tax computed as prescribed in Part I of the said Revenue Acts as the income of an individual.

5. The said Board erred in holding that the said declaration of trust, in so far as it provides that income shall be held and accumulated, is not in contravention of the laws of the State of California and void and of no effect.

6. The said Board erred in not holding that, in so far [52] as the said declaration of trust provides that income shall be held and accumulated, it is in contravention of the laws of the State of California, which require the petitioners to make immediate distribution of the said income and accumulation to the beneficiaries of the trust and under which said declaration of trust as affected by the said laws of the State of California the petitioners are required to file a return as a "trust" within the meaning of Section 219 of the said Revenue Acts of 1924 and 1926.

7. The decision of the said Board that the petitioners are taxable as an association is contrary to the evidence and is without evidence to support it.

WHEREFORE, the petitioners pray that this Honorable Court may review the opinion and decision of the Board and reverse and set aside the same and determine that no deficiencies in tax is due or owing by the petitioners in respect to the years 1924, 1925 and 1926; and that the Clerk of the United States Board of Tax Appeals shall be directed to certify, and transmit and deliver to the Clerk of this Honorable Court copies of all and every of the documents necessary and material to the presentation and consideration of this petition for review as required by the rules of this Honorable Court and the pertinent statutory provisions.

THEODORE B. BENSON,
917 Southern Building,
Washington, D. C.,
Counsel for Petitioners. [53]

District of Columbia—ss.

Theodore B. Benson, being duly sworn, on oath deposes and says that he is the attorney for T. A. Morrissey and James M. O'Brien, the petitioners above named; that he is duly authorized by said petitioners to verify the foregoing petition on their behalf; that he has read the foregoing petition and is familiar with the statements therein; and that the facts stated therein are true.

THEODORE B. BENSON.

Subscribed and sworn to before me this 22nd day of September, 1933.

CHARLES E. FOSTER, JR.
Notary Public, D. C.

[Endorsed]: United States Board of Tax Appeals. Filed, Sept. 23, 1933. [54]

NOTICE.

To E. Barrett Prettyman, General Counsel, Bureau of Internal Revenue, Counsel for Respondent.

You are hereby notified that on the 23rd day of September, 1933, a petition for review of the decision of the Board of Tax Appeals was filed with the Clerk in the case of T. A. Morrissey and James M. O'Brien, Trustees of an express trust, known as Western Avenue Golf Club v. Commissioner of Internal Revenue, Docket No. 40977, and a true copy of said petition is herewith served upon you.

THEODORE B. BENSON,
917 Southern Building,
Washington, D. C.,
Counsel for Petitioners.

Receipt of the above petition is hereby acknowledged this 23rd day of September, 1933.

E. BARRETT PRETTYMAN,
General Counsel,
Bureau of Internal Revenue,
Counsel for Respondent.

[Endorsed]: United States Board of Tax Appeals. Filed Sept. 23, 1933. [55]

[Title of Court and Cause.]

PRAECIPE FOR RECORD.

To the Clerk of the United States Board of Tax Appeals:

You will please prepare, transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause in connection with the petition for review by the said Circuit Court of Appeals for the Ninth Circuit, heretofore filed by the Petitioner:

1. Docket entries of the proceedings before the Board.
2. Pleadings before the Board,
   (a) The original petition.
   (b) The answer to the original petition.
   (c) Motion to amend petition and amendments to petition and order granting same.
   (d) Answer to amended petition.
3. Memorandum opinion of the Board. [56]
4. Decision of the Board.

5. Petition for review.
6. Stipulation of facts.
7. Petition for review, together with proof of service of notice of filing petition for review and of service of a copy of petition for review.
8. This praecipe.

THEODORE B. BENSON,
Attorney for Petitioner.

Service of a copy of the within praecipe is hereby admitted this 16th day of November, 1933.

E. BARRETT PRETTYMAN,
General Counsel,
Bureau of Internal Revenue.

[Endorsed]: United States Board of Tax Appeals. Filed Nov. 16, 1933. [57]

[Title of Court and Cause.]

CERTIFICATE.

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 57, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 18th day of December, 1933.

[Seal] B. D. GAMBLE,
Clerk,
United States Board of Tax Appeals. [58]

[Endorsed:] No. 7364. United States Circuit Court of Appeals for the Ninth Circuit. T. A. Morrissey and James M. O'Brien, Trustees of an Express Trust, known as Western Avenue Golf Club, Petitioners, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review an Order of the United States Board of Tax Appeals.

Filed January 2, 1934.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

No. 7364

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

T. A. MORRISSEY and JAMES M. O'BRIEN, Trustees of an Express Trust, Known as Western Avenue Golf Club,

Appellants,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Appellee.

Upon Petition to Review an Order of the United States Board of Tax Appeals.

PROCEEDINGS HAD IN THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

At a stated Term, to wit, the October Term, A. D. 1934 of the United States Circuit Court of Appeals for the Ninth Circuit, held in the Court Room thereof, in the City and County of San Francisco, in the State of California, on Tuesday the twenty-third day of October in the year of our Lord One Thousand Nine Hundred and thirty-four.

Present: Honorable CURTIS D. WILBUR, Senior Circuit Judge, Presiding, Honorable WILLIAM H. SAWTELLE, Circuit Judge, Honorable FRANCIS A. GARRECHT, Circuit Judge.

[Title of Cause.]

ORDER OF SUBMISSION.

ORDERED petition to review in above cause argued by Mr. Carlton Fox, Special Assistant to the Attorney General, counsel for respondent, and submitted on brief on file on behalf of petitioners, and submitted to the court for consideration and decision.

At a stated Term, to wit, the October Term, A. D. 1934 of the United States Circuit Court of Appeals for the Ninth Circuit, held in the Court Room thereof, in the City and County of San Francisco, in the State of California, on Monday, the seventh day of January in the year of our Lord One Thousand Nine Hundred and thirty-five.

Present: Honorable CURTIS D. WILBUR, Senior Circuit Judge, Presiding; Honorable FRANCIS A. GARRECHT, Circuit Judge.

[Title of Cause.]

ORDER DIRECTING FILING OF OPINION AND FILING AND RECORDING OF JUDGMENT.

By direction of the court, ORDERED that the typewritten opinion this day rendered by this court in above cause be forthwith filed by the clerk and that a judgment be filed and recorded in the minutes of this court in accordance with the opinion filed.

[Title of Court and Cause.]

OPINION.

Upon Petition to Review an Order of the United States Board of Tax Appeals.

Before: WILBUR and GARRECHT, Circuit Judges.

GARRECHT, Circuit Judge:

This petition for review involves deficiencies for income taxes in the sum of $1,890.55 for the year 1924, $1,623.49 for the year 1925 and $1,036.90 for the year 1926, and is taken from a decision of The Board of Tax Appeals. The question presented is whether or not the trust operated by the trustee petitioners was an "association" within the meaning of Section 2 [a] [2] of the Revenue Acts of 1924 and 1926.

Briefly stated, the facts are that on October 4, 1921, T. A. Morrissey and James M. O'Brien executed a declaration of trust to certain real estate in the city of Los Angeles, consisting of 155 acres of land, about one-third of which was subdivided into lots in 1921 and 1922, and which were all sold during said years. Such sales were apparently made on the installment basis, and were so treated by the Commissioner in determining the petitioners' income for the years 1923 to 1926, inclusive. On that portion of the tract not subdivided into lots the petitioner in 1922 constructed a golf course, which it thereafter operated until January 12, 1924. In the

meantime, however, in July 1923 petitioner sold the club to a corporation in exchange for all its capital stock and thereafter petitioners operated the same under a lease from said corporation. During 1924, 1925 and 1926 the petitioners received the sums of $53,560.65, $21,973.60 and $21,973.60, respectively, as dividends upon the said stock, all of which were returned as income by petitioners for the years in which they were received. Respondent, in his determination of the tax liability of petitioners eliminated said dividends from the taxable income of petitioners, for the years in which said dividends were so received, treating such dividends as nontaxable against petitioners as an association. The Board determined the petitioners to be an association for the years 1924, 1925 and 1926, and assessed taxes as above stated.

The trust instrument, among other things, authorized the trustees to take and hold not only the property in question, but any and all other property, real, personal or mixed which might thereafter be conveyed or transferred to or acquired by them, and in separate paragraphs from a to z the trust instrument authorized the trustees to engage in all manner of business activities. The instrument further provides that during the continuation of the trust the beneficial interest therein shall be solely evidenced by certificates or shares; that certificates for several thousand shares, at the par value of $100, were issued; that between 1922 and 1926 the number of interest holders varied from 275 to 920.

Exclusive management was vested in the trustees, the shareholders' interest being to receive dividends as declared.

The activities of the petitioners, according to the stipulation of facts, during the years 1924, 1925 and 1926 were confined to

> "* * * (1) Operation of said golf course for the first 12 days of 1924 as aforesaid; (2) Receipt from collection agent bank of principal and interest so collected by said bank in behalf of petitioner; (3) Receipt of credit of interest earned on bank balances; (4) Receipt of assignment fees in assignment of lot-purchase contracts by holders thereof; (5) Conveyance of lots to purchasers thereof; (6) Receeipt of dividends from Western Avenue Golf Club, Inc., upon shares thereof owned by petitioner; (7) Distribution of moneys to holders of beneficial interests in petitioner trust by way of dividends and, in some cases, by way of redemption and retirement of their beneficial interests. * * *"

Section 2 [a] [2] of the Revenue Act of 1924, which is applicable to the tax for the year 1924, and the same numbered section of the Revenue Act of 1926, which is applicable for tax for the years 1925 and 1926, are identical, and each act reads as follows: "The term 'corporation' includes associations joint stock companies and insurance companies."

The question for this court to determine is whether the petitioners' trust was an association, taxable as a corporation for the taxable years in question, as determined by respondent, and as found by the Board, or a strict trust, as contended by the petitioners.

The petitioners contend that the declaration of trust under which they are trustees did not create an association within the meaning of the term as used in the several Revenue Acts. They argue that they were not engaged in business; that the element of "doing business" was neither relevant or a controlling factor in the determination of whether a trust is taxable as an association; that there was no such beneficiary control as was necessary to classify petitioners as an association.

The contention of petitioners, that the trust was not engaged in business in the tax years here in question, because its activities in those years had been reduced to the collection of installments and dividends, to the necessary conveying of property previously sold, and the like, is answered to the contrary by the decision of this court in the case of Sloan v. Commissioner, 63 F. (2d) 666 [C. C. A. 9].

As to the contention that "doing business" is not controlling or relevant, this court in Twin Bell Oil Syndicate v. Helvering, 70 F. (2d) 402 [C. C. A. 9], after quoting from its opinion in the Trust No. 5833, Security First National Bank v. Welch, 54 F. (2d) 323 [C. C. A. 9], said at page 407:

"There is ample additional authority for the proposition that the 'business' test is now paramount."

Concerning petitioners' contention that the trust in question here is not an association because there is no beneficiary control, it may be said that on a misconception of Crocker v. Malley, 249 U. S. 223, the Treasury Department promulgated regulations providing that beneficiary control was a prerequisite for holding a trust to be a corporation. However, since the decision in Hecht v. Malley, 265 U. S. 144, the Department changed its regulations and rulings, making proof of beneficiary control unnecessary. Congress thereafter recognized and validated this change in the ruling by Section 704(a) of the Revenue Act of 1928, the force of such change being pointed out in Sloan v. Commissioner (supra), and Trust No. 5833, Security First National Bank v. Welch (supra). It is now well settled that beneficiary control is not a requisite to the taxability of a trust as a corporation. Twin Bell Oil Syn. v. Helvering (supra).

Petitioners further contend that Section 704(b) of the Revenue Act of 1928 is unconstitutional as an arbitrary exclusion of petitioners from the benefit of said sub-section, because it has two trustees instead of having a single trustee. There is no merit in this contention. This law provides that besides having but a single trustee the trust must be

"* * * created and operated for the sole purpose of liquidating real property as a single

venture (with such powers of administration as are incidental thereto, including the acquisition, improvement, conservation, division, and sale of such property), distributing the proceeds therefrom in due course to or for the benefit of the beneficiaries, and discharging indebtedness secured by the trust property * * *".

As under the facts found and the determination thereof the trust here in question is not a liquidating trust, and thus in any event petitioners would not be entitled to the benefit of said section.

The decision of the Board of Tax Appeals is affirmed.

(Endorsed): Opinion. Filed Jan. 7, 1935. Paul P. O'Brien, Clerk.

United States Circuit Court of Appeals for the Ninth Circuit.

No. 7364

T. A. MORRISSEY and JAMES M. O'BRIEN; Trustees of an Express Trust, known as Western Avenue Golf Club,

Appellants,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Appellee.

JUDGMENT.

Upon Petition to Review an Order of the United States Board of Tax Appeals.

This Cause came on to be heard on the Transcript of the Record from the United States Board of Tax Appeals and was duly submitted.

On Consideration Whereof, it is now here ordered and adjudged by this Court, that the Order of the said Board of Tax Appeals in this Cause be, and hereby is affirmed.

[Endorsed]: Filed and entered Jan. 7, 1935. Paul P. O'Brien, Clerk.

At a stated Term, to wit, the October Term, A. D. 1935 of the United States Circuit Court of Appeals for the Ninth Circuit, held in the Court Room thereof, in the City and County of San Francisco, in the State of California, on Friday the first day of March in the year of our Lord One Thousand Nine Hundred and thirty-five.

Present: Honorable CURTIS D. WILBUR, Senior Circuit Judge, Presiding, Honorable FRANCIS A. GARRECHT, Circuit Judge.

[Title of Cause.]

ORDER DENYING PETITION FOR A REHEARING.

Upon consideration thereof, and by direction of the court, IT IS ORDERED that the petition of petitioners, filed February 5, 1935, for a rehearing of above cause be, and hereby is denied.

[Title of Court and Cause.]

ORDER STAYING ISSUANCE OF MANDATE.

Upon application of Theodore B. Benson counsel for the Petitioners, and good cause therefor appearing, IT IS ORDERED that the issuance, under Rule 32, of the mandate of this Court in the above cause be, and hereby is stayed to and including April 1, 1935; and in the event the petition for a writ of certiorari to be made by the counsel for petitioners herein be docketed in the Clerk's office

of the Supreme Court of the United States on or before said date, then the mandate of this Court is to be stayed until after the said Supreme Court passes upon the said petition.

CURTIS D. WILBUR,
Senior United States Circuit Judge.

Dated: San Francisco, California,
March 1, 1935

[Endorsed]: Filed Mar. 1, 1935. Paul P. O'Brien, Clerk.

[Title of Court and Cause.]

CERTIFICATE OF CLERK U. S. CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT TO RECORD CERTIFIED UNDER RULE 38 OF THE REVISED RULES OF THE SUPREME COURT OF THE UNITED STATES.

I, PAUL P. O'BRIEN, as Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, do hereby certify the foregoing seventy-five (75) pages, numbered from and including 1 to and including 75, together with supplemental transcript of record consisting of 40 pages, numbered from and including 1 to and including 40, to be a full, true and correct copy of the entire record, of the above-entitled case in the said Circuit Court of Appeals, made pursuant to request of counsel for the petitioners and certified under Rule 38 of the Revised Rules of the Supreme Court of the United States, as the originals thereof remain on file and appear of record in my office.

ATTEST my hand and seal of the said the United States Circuit Court of Appeals for the Ninth Circuit, at the City of San Francisco, in the State of California, this 16th day of March, A. D. 1935.

[Seal] PAUL P. O'BRIEN,
Clerk

CLERK'S COPY.

Vol. II

SUPPLEMENTAL TRANSCRIPT OF RECORD

Supreme Court of the United States

OCTOBER TERM, 1935

No. 17

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES OF AN EXPRESS TRUST KNOWN AS WESTERN AVENUE GOLF CLUB, PETITIONERS,

vs.

COMMISSIONER OF INTERNAL REVENUE.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

PETITION FOR CERTIORARI FILED APRIL 1, 1935.

CERTIORARI GRANTED MAY 13, 1935.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1935

No. 17

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES OF AN EXPRESS TRUST KNOWN AS WESTERN AVENUE GOLF CLUB, PETITIONERS,

vs.

COMMISSIONER OF INTERNAL REVENUE.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

VOL. II.

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JUDD & DETWEILER (INC.), PRINTERS, WASHINGTON, D. C., AUGUST 20, 1935.
—6792-C

VOL. II

EXHIBIT "B"

WESTERN AVENUE GOLF CLUB
DECLARATION OF TRUST

We, T. A. Morrissey and James M. O'Brien, both of Los Angeles, in the County of Los Angeles, State of California, hereby declare that we will and our successors shall hold the following described property, to-wit:

> The Southeast quarter of Section Twenty-six (26), Township 2 South, Range 14 West, S. B. B. & M. in the above mentioned City, County and State, excepting the east half of the southwest quarter of the southeast quarter of said southeast quarter,

which property has already been conveyed to us, and also any and all other property, real, personal, or mixed, which may hereafter be conveyed or transferred to or acquired by us or them as trustees hereunder, together with the proceeds and avails thereof in trust upon the trusts hereinafter set forth to maintain and to dispose of the same, and to collect, receive, hold and distribute the net income thereof for the benefit of the beneficiaries from time to time, whose beneficial interests in said property are represented by certificates for shares of beneficial interest issued hereunder according to the number of such shares held by them respectively, and in accordance with the priorities hereinafter expressed, and in the

manner and subject to the stipulation herein contained, to-wit: [1*]

1. Wherever the term trustees is used herein it is intended to include and shall be construed to include the undersigned trustees and their successors in trust; wherever the term shareholder is used herein it is intended to include and shall be held to include any holder of a certificate evidencing a share or shares of beneficial interest issued hereunder and the successor in interest of the holder of such certificate.

2. The trustees in their collective capacity shall be designated as "WESTERN AVENUE GOLF CLUB", or by such other designation or name as the trustees may adopt, and under such name and so far as may be practicable and convenient, shall manage and administer the trust estate, execute all their instrments of writing, and do all other things relating to the trust hereby created; and every duly authorized instrument executed in the name of "WESTERN AVENUE GOLF CLUB", or any such other designation or name as may hereafter be adopted by the trustees, shall have the same effect as if executed in the names of the trustees as such.

3. The trustees shall be two in number, except and until the number of trustees shall have been increased and the persons hereinbefore mentioned and who execute this declaration of trust, shall be and shall constitute the original trustees.

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*Page numbering appearing at the foot of page of original certified Transcript of Record.

4. At any time and from time to time the trustees may increase the number of trustees, in which event the persons to fill the places thus created shall be selected and their successors shall be selected by a majority of the trustees in office at the time of such selection.

5. Whenever a vacancy from death, resignation, inability to serve, or removal, occurs among the Trustees, then the Trustees then in office as such, shall elect the successor Trustee to fill the vacancy thus created, and this right shall continue at all times; it being hereby intended that the right to select Trustees in the manner hereinabove indicated shall not be exhausted by any one or more exercises thereof, but that such right, so far as the said Trustees are concerned, shall continue during the existence of this trust.

6. As soon as any trustees so selected under the provisions of either of the two preceding paragraphs shall have accepted the terms of this trust by an instrument in writing executed in duplicate if required, and delivered to the continuing trustees, the trust estate shall forthwith vest in the continuing trustees and in such new trustees or trustee without any further act or conveyance, with all the right, title, interest, privileges, powers, duties and estate which the former trustee or trustees possessed during his or their incumbency, to the same extent as if such newly selected trustee or trustees had been the original and first trustee or trustees under this trust. [2]

7. Any trustee may resign his office of trust hereunder by a written instrument acknowledged in the manner prescribed for the acknowledgment of deeds, and by sending the same by registered mail to the continuing trustees or one of them, and by executing and delivering to the continuing trustees such instrument or instruments in writing quit-claiming to the continuing trustees as such all right, title and interest of said resigning trustee as such in any part of the trust estate.

8. Where there are more than two trustees a majority only shall be necessary to unite in any act to bind the trust property; where there are only two trustees both must unite in any act to bind the trust property.

9. The trustees are authorized:

(a) To purchase, buy, own, hold, encumber, contract for, take title to, deal with or otherwise acquire the above described or other lands, tenements, hereditaments and real property of all kinds, and any interest therein, and to sell, convey, transfer, quitclaim, assign, set over, encumber, mortgage, pledge, exchange, contract to sell, or otherwise deal with and dispose of the above described or other lands, tenements, hereditaments, and real property of all kinds, and any interest therein, upon such terms and for such consideration, whether for cash or for securities, or upon credit, as and whenever the trustees in their absolute discretion may deem proper. To rent, lease and assign or license the use of the above described or any other lands, tene-

ments, hereditaments and real property, and any interest therein, upon such terms and consideration as and whenever it may be deemed wise and proper by the trustees in their sound discretion. To farm, till, operate, work and cultivate, or to cause or permit to be farmed, tilled, operated, worked and cultivated, the above described or any other lands or real estate, upon such terms and conditions, and for such considerations and remunerations, whether for cash or securities or for fixed or contingent returns, whether cash or in commodities and merchandise, as and whenever in the absolute discretion of the trustees may seem advisable and proper.

(b) To construct or acquire and operate, maintain and repair golf courses, tennis courts, swimming pools, bowling alleys and clubhouses, and stores, shops, cafes, and other businesses incidental thereto, and to charge and receive fees, profits and emoluments in connection with any of said operations, and to sell or dispose of upon such terms or conditions as the trustees in their discretion may determine such rights or concessions in connection with any of said operations as they may determine.

(c) To manage and control the trust estate, and receive rents, profits, proceeds, income and avails thereof, whether from [3] or in the form of real property, personal property, or mixed property, and in connection therewith to buy, discount or otherwise acquire, hold, own, invest in, deal in, accept, guarantee, endorse and sell, assign, mortgage, pledge, exchange, have discounted and otherwise deal with or dispose of, upon such terms and for such considera-

tion, whether for cash or for other securities, as the trustees in their absolute discretion may deem proper, shares of stock, participation shares, trust certificates, certificates of interest, bonds or securities of corporations, trusts, trustees, or associations in whatsoever business engaged, commercial paper, commercial securities, promissory notes, leases, mortgages, conditional sales, open accounts receivable, book debts and claims, acceptances, drafts, foreign and domestic bills of exchange and bills of lading, finance bills, warehouse receipts, trust receipts, warrants, contracts and choses in action of every kind and description, whether issued, made or owned by, or existing in favor of, or against, individuals, corporations, associations, trusts or trustees, either with or without recourse.

(d) To make loans or advances to any person, firm, corporation or association of any moneys or other valuable things forming a part of the trust estate, without collateral security, or to take as collateral security for the payment of any such loans or advances, such real, personal or mixed property or rights or choses in action as the trustees in the exercise of an absolute discretion may desire; to grant, procure, extend and guarantee credits, loans and investments, and to indorse or otherwise assure credits, loans and investments, and to indorse or otherwise assure and guarantee the payment and re-payment thereof, with or without collateral security; and to act as trustee or otherwise for the securing of loans and investments and the financing thereof.

(e) To become guarantor and surety upon letters of credit, open accounts, acceptances, drafts, notes, foreign and domestic bills of exchange, contracts and agreements of every kind and description, whenever the Trustees in their management of the trust estate deem it advisable or expedient so to do, to promote, protect and conserve this trust and interests of the beneficiaries and, whenever the Trustees in their absolute discretion deem it advisable for the purpose of increasing the income of the trust estate, and of promoting, protecting and conserving the property constituting the trust estate or part thereof, to act as brokers, factors, agents, trustees, managers, receivers, liquidators and attorneys in fact and as organizers and reorganizers of enterprises requiring financing.

(f) To vote or cause to be voted any shares of stock, certificates of interest, bonds, or other securities of corporations, trusts or associations, at the time forming any part of [4] the trust estate; to assign to any person or persons such shares, certificates, bonds or securities, and to allow the same to stand in the name or names of such person or persons so long as the trustees shall think proper, for the purpose of qualifying such person or persons as a director or directors, or as trustee or trustees, or as an officer or officers of such corporations, trusts or associations or otherwise, for the purpose of maintaining the organization of such corporations, trusts, associations, or for any other purpose deemed expedient by the Trustees; and to cause such shares of stock, certificates of interest, bonds or other

securities at the time forming any part of the trust estate to be transferred into the names of or vested in the Trustees or any of them jointly, with the right of survivorship in any one of them in such manner as not to give notice that they are trustees thereof, or that the same are effected by any trust, or to allow or cause such shares of stock, certificates of interest, bonds or other securities to remain in or to be transferred to the name or names of any other persons, firm, association, trust or corporation, and to entrust to any bank or trust company or safe deposit company for safekeeping any or all of the certificates of stock, bonds, securities, claims and all documents and paper comprised in or relating to the trust estate.

(g) To collect and sue for, and to receive and receipt for, all moneys due to the trustees; to represent the beneficiaries hereunder in all suits and legal proceedings in any court of law or equity, or before any body or tribunal; to commence suits and legal proceedings and to defend same for the purpose of protecting and conserving the interests of the trust estate, the trustees or the beneficiaries, and to employ counsel; to compound, compromise, abandon or adjust by arbitration or otherwise any action, suits, proceedings, disputes, claims, demands and things relating to the trust estate, and to give time, with or without security, for the payment or delivery of any debts or property claimed in favor of the trust estate, and to pay or satisfy any debts or claims, upon any evidence that the trustees may deem sufficient.

(h) To buy or join with any person, firm, corporation or association in buying the property of any person, firm, corporation, trust or association, any of the securities which are included in the trust estate, or any property in which the trustee, as such, shall have or may hereafter acquire an interest, and to allow the title to any property so bought to be taken in the name or names of, and to be held by, such person or persons as the trustees shall name or approve.

(i) To procure such insurance for the protection of the trust estate against loss or liability as the trustees may in the exercise of their absolute discretion decide, including [5] policies or bonds protecting against loss by fire, theft, liability, infidelity, injury or death to any trustee, officer or employee, or any other insurable risk, and to pay out of the trust estate necessary premium therefor.

(j) To hold or invest from time to time any moneys under the control of the trustees by them deemed to be available for the purpose, in any security or property which the trustees may select or approve, in the same manner and to the same extent as if they were not trustees, but making such investment as natural persons, without any limitation in respect of the character of the securities invested in, and to sell or otherwise dispose of any such investments and reinvest the proceeds thereof, or make, execute and issue either in person or by one or more of their duly authorized officers, representatives, agents or employees, any notes, drafts,

acceptances, bills of exchange, finance bills, bonds or debentures, with or without security; to enter into any and all contracts, guaranties, obligations and other instruments which in the opinion of the trustees may be necessary or expedient to carry out, promote, protect and conserve the trust estate, including the making of guaranties to secure the performance of contracts and obligations of other parties; and to charge the trust estate with any and all obligations of indebtedness incurred by the trustees in the exercise by them of any or all of the foregoing powers conferred upon them; provided, however, the trustees shall have no power or authority whatsoever to borrow money on the credit of the beneficiaries, or to make any contract on their credit for repayment of any money raised by mortgages, pledge, charge or other encumbrances in pursuance of the provisions hereof, or to make any contract or to incur any liability whatsoever binding the beneficiaries personally.

(o) Generally, to do all and singular, such things as may be necessary or advantageous in the execution of the foregoing powers, or any of them, and not inconsistent therewith, and to manage and conduct the affairs of the trust estate as fully as if the trustees were the absolute owners of the trust estate; and to make and execute and do all such agreements, deeds, instruments and things as they may deem proper in the execution of any of the said powers.

(p) The foregoing clauses shall be construed both as objects and powers and no enumeration of specific powers herein found shall be held to limit or restrict the powers of the trustees in any manner unless expressly so provided or clearly implied herein; to vest in and delegate to any trustees or committees selected from their own number, and [6] to officers, representatives, including counsel, agents and employees, such powers and authority conferred upon the trustees by this declaration as the trustees may specify, and to alter, modify or revoke any such grant or delegation of powers and authority at discretion.

(q) To make, change, revoke and rescind such rules and regulations, not inconsistent with the terms of this instrument, as they deem necessary or desirable for the management of any part of the trust estate and for the management of themselves, their committees, officers, representatives, directors, agents and employees; to adopt and use a common seal, but such seal may or may not be affixed to instruments executed by the trustees, executive committee, or the officers of the trust, and the absence of such seal shall in nowise effect the validity of such instruments; to remove any trustees (except the original trustees) officer or member of any committee, when in the judgment of the trustees the interests of this trust shall so require. Such removal shall create a vacancy which shall be filled in the manner herein prescribed; to appoint an advisory board consisting of not to exceed fifteen (15) per-

sons, who shall be known as Directors, but the appointment of such advisory board shall not be construed as limiting any of the powers of the trustees hereunder.

(r) To appoint an Executive Committee consisting of three (3) persons selected from such Advisory Board, who shall act for said Board when the full Board is not in session, or when it may not be convenient to call a meeting of said Advisory Board.

(s) To appoint and designate from amongst their own number or otherwise such executive officers to furnish them assistance in the management of the trust, including a president, and one or more vice presidents, a secretary, a treasurer, and such other officers as the trustees may from time to time deem expedient, and to define their respective duties, and said duties so defined may be any or all the trustees may possess hereunder; any person so appointed may hold more than one office.

(t) To remove, or discharge any or all members of the Advisory Board or Executive Committee or persons holding any of said offices and to abolish such Advisory Board or Executive Committee or any of said offices at any time.

(u) To employ, remove, or discharge such other representatives, agents and employees of any kind as the trustees may deem proper.

(v) To define the tenure of office or employment of all officers, representatives, agents and employees, and to define their duties and to fix and pay their compensation out of the trust estate. [7]

(w) The naming of any specific duties and powers herein shall not be construed as limiting the general powers conferred upon the trustees by this Agreement and Declaration of Trust, such powers shall continue during the existence of this trust, and shall not be exhausted by one or more exercises thereof; the trustees shall hold the legal title to, and have the absolute and exclusive control of, all property at any time belonging to this trust, and they shall have the absolute control, management nd disposition thereof.

(x) The trustees may, and the directors and Executive Committee shall hold meetings at such time or times and at such place or places and upon and after notice given in such manner and for such time as the trustees may at any time hereafter and from time to time hereafter determine upon; a majority of the trustees, director or executive committee shall constitute a quorum at any of their respective meetings; any action finally taken or authorized by a majority of all the then trustees shall be valid, and when so authorized must be performed.

(y) The death or resignation of the trustees or any of them shall not operate to annul or terminate this trust, or to revoke any existing agency created pursuant to the terms of this instrument.

10. The trustees, officers, representatives, agents and employees actively engaged in managing the trust estate or rendering services in connection therewith, shall be entitled to receive and shall be

paid such remuneration from the trust estate or the income thereof as from time to time shall be fixed or agreed upon by the trustees. The trustees shall be reimbursed from the trust estate for their expenses and disbursements, including counsel fees, and also in respect of all losses and liabilities by them incurred in administering this trust, and for the payment of such compensation, expenses, disbursements, losses and liabilities the trustees shall have a lien on the trust estate prior to any rights or interest of the beneficiaries thereto or herein.

11. The receipt of the trustees or any of them or any of their representatives, agents or employees thereunto authorized, for moneys or property paid or delivered to them or any of them, shall be an effectual discharge therefrom to the person paying or delivering the same, and no person taking such receipt shall be bound to see to the application of such moneys or property. And no purchaser or person dealing with the trustees shall be bound to ascertain or inquire as to the existence or occurrence of any event or purpose in or for which sale, mortgage, pledge or charge is herein authorized or directed or otherwise as to the purposes or regularity of any of the [8] acts of the trustees, or any of them, purporting to be done in pursuance of any of the provisions or powers herein contained, or as to the regularity of the removal, resignation, or selection of any trustees. And no purchaser or person dealing with any trustee purporting to act under any delegation of authority from the trustees shall be required to

ascertain or inquire whether an occasion exists in which he is authorized so to act, or in which such delegation is permitted, or whether such delegated authority is still subsisting.

12. Every note, bond, contract, instrument, certificate or undertaking, and every other act or thing whatsoever executed or done by the trustees, or any of them, in connection with this trust, shall be conclusively taken to have been executed or done only in their or his capacity of trustee or trustees under this Agreement and Declaration of Trust, and such trustees or trustee shall not be personally liable thereon. Every such note, contract, bond, instrument, certificate or undertaking made or issued by the trustees shall recite that the same is executed or made by them, not individually but as trustees under this Agreement and Declaration of Trust, and may contain any further recital which they or he may deem appropriate.

13. The trustees shall have no power to bind the beneficiaries personally by any act, neglect or default, and all beneficiaries and all persons, corporations, trusts or associations extending credit to, contracting with, or having any claim against the trustees, shall look only to the funds and property of this trust for payment of such contract or claim or for any indemnity or for the payment of any debt, damage, judgment or decree, or of any money that may otherwise become due or payable from the trustees, so that neither the trustees, directors, executive committee, beneficiaries, nor the officers,

representatives, agents and employees of the trustees, present or future, shall be personally liable therefor.

And any written obligation, contract or undertaking made or issued by the trustees may provide expressly, in substance or effect, as follows:

> "This obligation (contract or undertaking, as the case may be) is made (or issued) by the undersigned, not individually but as trustees under a certain trust agreement creating the WESTERN AVENUE GOLF CLUB, dated September 25, 1921, and hereby made a part hereof, and is enforceable only against, and is payable only out of, the trust property held thereunder, any and all personal liability of the trustees and beneficiaries thereunder being and having been expressly waived by the holder hereof." [9]

14. The trustees shall not be liable for errors of judgment in exercising any of their powers of discretions hereunder or in the appointment of any succeeding or other trustee or officer, director, representative, agent or employee, nor for any loss arising out of any investment made in good faith by the trustees, nor for failure to sue for or to collect or to invest any moneys or property belonging to this trust, or to require security for any investment, or for any act or omission to act performed or omitted by them in the execution in good faith of their powers or discretions hereunder; each trustee shall be answerable and accountable

only for his own several acts, receipts, neglects, and defaults severally and respectively, and not for those of any other trustee or of any of the directors, officers, representatives, agents and employees of the trustees or any of them, or for any bank, trust company, broker or actioneer or other person with whom or into whose hands any trust moneys, property or securities may be deposited or come.

15. Any trustee may acquire, own and dispose of shares of beneficial interest in this trust to the same extent as if he were not a trustee. Any trustee, notwithstanding the fiduciary position which he holds, may serve and deal with the trustees in relation to the trust estate as freely, and be entitled to compensation for services as if he were not a trustee hereunder.

16. No recourse at any time shall be had under or upon any note, bond, contract, instrument, certificate, undertaking, obligation, covenant or agreement issued or executed by the trustees under or pursuant to the terms of this Agreement and Declaration of Trust, or in managing the trustee estate, or by the executive committee or any member thereof, or by any officer, representative, agent or employee of the trustees, or by reason of anything done or omitted to be done by them or any of them, against the trustees individually, or against the members of the executive committee, or any of them, or against any such officer, representative, agent or employee against any beneficiary or the holder of any other security issued by the trustees, either

directly or indirectly, by legal or equitable proceedings, or by virtue of any suit or otherwise, except only to compel the proper application or distribution of the trust estate, it being expressly understood and agreed that—

(a) This Declaration of Trust, and all obligations and instruments executed thereunder, are executed pursuant thereto by the trustees; that—

(b) Any acts done or omitted to be done by them are solely the obligations, instruments, acts and omissions of, or in respect of, the trust estate, and that— [10]

(c) All the obligations, instruments, liabilities, covenants, and agreements, acts and omissions of the trustees as trustees shall be enforced against, and shall be satisfied out of, the trust estate only, or such part thereof as, under the terms and provisions of the Agreement and Declaration of Trust, shall be liable for or chargeable therewith. And all personal and individual liability of the trustees, except as above stated, and of the members of the executive committee, and of all officers, representatives, agents and employees, and of the beneficiaries of this trust, are hereby expressly waived and negatived. Neither the trustees nor their representatives, agents or employees are authorized to contract any debt or do anything which will charge the beneficiaries or bind them personally.

17. No corporation, trust, association or body politic shall be affected by notice that any of its shares of stock, certificates of interest, or bonds or

other securities are subject to this trust, or be bound to see to the execution of this trust, or to ascertain or inquire whether any transfer of any such shares, bonds or securities by the trustees is authorized by this trust, notwithstanding such authority may be disputed by some other person.

18. During the continuance of this trust the beneficial interests therein and thereunder shall be solely evidenced by certificates for shares of beneficial interest for which provision is hereinafter made.

19. Such beneficial shares shall be divided into two thousand (2,000) preferred shares of the par value of One Hundred ($100.00) Dollars each, and two thousand (2,000) common shares of no par value.

20. The holders of record upon the books of this trust of outstanding preferred shares shall be entitled to receive when and as declared by the trustees out of the surplus profits arising from the business of this trust, or surplus, dividends at the rate of $8.00 per share per annum without preference of priority one over the other, before any dividend shall be declared or set aside or paid on the common shares; the said dividends upon the said preferred shares shall be cumulative from and after the date of issuance thereof, and until redemption or retirement thereof; at any time and from time to time when holders of outstanding preferred shares shall have received, or there shall have been reserved for them up to date, all cumulative dividends to

which they may be then entitled hereunder, and when any surplus profits or *surplus profits or* surplus remain thereafter, the holders of record [11] of common shares then outstanding shall be entitled to receive when and as declared by the trustees out of the surplus profits arising from the business of said trust, or surplus, dividends at such rate as may be determined and decided upon by the trustees in the exercise of their absolute discretion, not exceeding the rate of $8.00 per share per annum, but without preference or priority as to said common shares one over the other.

21. If at any time any surplus profits arising from the business of the trust, or any surplus shall remain in the hands of the trustees after there shall have been paid or reserved for payment to the preferred shareholders, all cumulative dividends to which they may then be or theretofore have been entitled out of the surplus profits arising from the business of said trust, or out of the surplus thereof, and after there shall have been paid or reserved for payment to the holders of common shares dividends out of said surplus profits or surplus, equal in amount per share to the dividends per share theretofore paid and then reserved for payment to the holders of preferred shares, the trustees may, in the exercise of an absolute discretion, declare and pay out of such remaining surplus profits and surplus such extra dividends upon the preferred shares and upon the common shares as said trustees may decide and determine, such dividends to be declared, paid, and

distributed to the holders of then outstanding preferred shares, and to the holders of then outstanding common shares, share and share alike, and ratably, and without preference or priority one over the other.

22. In the distribution of the capital assets of the trust upon the liquidation of the affairs thereof as a whole, there shall be first apportioned to the holders of preferred shares then outstanding, out of surplus profits arising from the business of the trust, or surplus, if any such surplus profits or surplus then remain or exist, all or so much of the cumulative dividends at the rate aforementioned as then remain unpaid, if any; if any such surplus profits or surplus are available but insufficient for the purpose last mentioned, then the said distribution thereof to preferred shareholders shall be ratable and without priority or preference as to such preferred shares one over the other; for the purpose of this paragraph only and to determine what, if any, surplus profits or surplus are available after but not before liquidation, the common shares shall be considered as having a tentative par value of $100.00 per share and the amount of outstanding common shares computed on that basis added to the gross par value of all then outstanding preferred shares shall represent the capital stock liability in determining the net assets for such purposes; in case such surplus profits shall be more than [12] sufficient to pay the preferred shareholders all of such unpaid accumulations of dividends, and in case the dividends

then and theretofore paid per share upon preferred shares shall have been in excess of the dividends per share paid upon the common shares, then the remaining surplus profits shall be apportioned to the holders of then outstanding common shares to such extent as would then bring the gross payments of dividends to common shareholders per share up to the gross dividends per share then and at all times theretofore, both before and during such liquidation, received by preferred shareholders; in event any such surplus profits or surplus shall be available but insufficient for the purpose last above mentioned, the said distribution thereof to common shareholders shall be ratable, share and share alike and without preference or priority as to said common shares one over the other; and in event they shall be more than sufficient for that purpose the balance thereof shall be considered capital assets. The capital assets shall thereafter be distributed as follows, to-wit:

(a) There shall be first apportioned to the holders of preferred shares then outstanding in cash or otherwise, the par value of said preferred shares before any of said capital assets shall be distributed to or apportioned to the holders of common shares; if the capital assets shall be insufficient to pay to the holders of preferred shares the total par value thereof, as aforesaid, such capital assets shall be distributed to the holders of said outstanding preferred shares, share and share alike, ratably, and without preference or priority one over the other; in

case the capital assets shall be more than sufficient to pay to the holders of then outstanding preferred shares the full par value thereof, as aforesaid, then the remainder of such capital assets shall be apportioned to the holders of common shares then outstanding to the extent of $100.00 per share; if there shall be insufficient capital assets for that purpose last mentioned the apportionment to such common shareholders shall be ratable, share and share alike, and without preference or priority one over the other; if there shall be more than sufficient capital assets for the said purpose the remainder thereof after apportioning the then outstanding common shareholders the sum of $100,00 per share in cash or otherwise, as aforesaid, shall be distributed and apportioned to the holders of preferred shares then outstanding, ratably, share and share alike and without preference or priority one over the other.

23. The preferred shares shall be non-assessable; the common shares shall be assessable for all purposes contemplated by Section 26 hereof, other than and except the purposes of raising moneys to apportion or distribute to the holders of preferred shares, either by way of dividends or otherwise, [13] and no funds raised by assessment upon the common shares shall be so used; assessments upon the common shares shall be levied only if, as and when decided to be necessary or advisable by the trustees in the exercise of their absolute and exclusive discretion and they shall not be compellable to levy

and collect any assessment. All assessments levied and collected upon common shares shall be carried on the books as a contingent liability to the common shareholders who paid the same, and must be repaid, or funds reserved for repayment thereof, to such shareholders before any dividends, either regular or extra, may be thereafter declared or paid upon any shares, either preferred or common, and before any capital assets may be distributed or paid to any shares, either preferred or common.

24. Any and all dividends and apportionments of capital assets shall be payable only to the holders of then outstanding shares as shown upon the books of the trust and the trustees shall have no liability to any other claimant; payment or distribution of capital assets, as aforesaid, shall be made only upon the surrender and cancellation of the certificate evidencing the shares involved or upon the record owner thereof indemnifying the trustees to such extent and in such manner as the trustees may require against loss resulting from any subsequent production of any lost or destroyed certificates; after the trustees shall have determined to wind up the affairs of the trust they shall fix a liquidation date as of which the liquidation shall become effective and shall give notice for such time and in such manner to the shareholders of record as the said trustees may in the exercise of an absolute discretion decide and determine upon, and all dividends shall cease to accrue and to accumulate upon and after such liquidation date, whereafter any capital assets remaining undistributed on account of the failure of any share-

holder to produce his certificate as required hereinbefore shall be held by the trustees as trustee for such shareholder, without any liability whatever upon said trustees therefor, or for the investment thereof, or for any income thereon, or for any loss from any cause except willful malfeasance upon the part of the said trustee.

25. So long as any of said preferred shares may remain outstanding the trustees shall not issue any shares which shall have any preference to or take priority over the preferred shares hereinbefore authorized, nor issue preferred shares on a parity with those hereinbefore authorized in excess of the number of preferred shares hereinbefore authorized, nor alter in any manner the rights or preferences herein granted to the preferred shares hereinbefore authorized, but subject to these limitations the trustees may at any time and from time to time, as they in the exercise of an absolute discretion, may decide and determine upon, increase the number of common shares over and above the number hereinbefore authorized, and issue preferred shares junior in right to those hereinbefore authorized, and of such par value, if any, and in such amount [14] and number as the said trustees may desire, and issue such bonds, collateral, trust certificates and other evidences of indebtedness as the said trustees in the exercise of their sound discretion may determine and decide upon.

26. The trustees may at any time hereafter and from time to time levy and collect assessments upon the outstanding common shares for the purpose of paying expenses, conducting business or paying

debts in the manner and form and to the extent provided by the Civil Code of the State of California, for the levying and collection of assessments by private corporations organized for profit, as such provisions of the Civil Code may from time to time be amended, with these sole changes, to-wit:

First: The trustees shall not be limited at any time in the amount of any assessment which they may levy and collect.

Second: An assessment may be levied and its collection enforced notwithstanding the whole or any portion of an assessment previously levied remains unpaid.

Third: The order levying the assessment shall be valid and binding if signed by a majority of the trustees then in office without the requirement of any meeting for that purpose.

Fourth: Notice of assessment need not be published in any newspaper, or posted.

Fifth: Notice of delinquent sale need not be published in any newspaper, or posted.

Sixth: The sole liability on the part of the shareholders for non-payment of assessments shall be the sale of their shares and there shall be no personal liability on the part of any of such shareholders for the payment of any of said assessments or any part thereof, and the trustees shall not have power to proceed by action or otherwise to recover the amount of assessment of costs individually from any shareholder, but shall be limited to the proceedings for the sale of any of such shares for non-payment of such assessment.

Seventh: Notice of assessment given personally or by ordinary mail to any shareholder at least five days prior to the delinquent date shall be sufficient as to such shareholder, and that notice of delinquent sale given personally or by ordinary mail to any shareholder who may be delinquent in the payment of any assessment at least five days before the day fixed for the sale of delinquent shares shall be sufficient as against said delinquent shareholder so notified. [15]

Eighth: Any shareholder so notified of the levy of the assessment shall be estopped from asserting the invalidity thereof on account of lack of notice to any other shareholder, and any shareholder so notified of any intended sale of his delinquent shares shall be estopped from asserting the invalidity of any sale on account of the lack of such notice to any other delinquent shareholder.

27. The trustees may at any time and from time to time hereafter purchase in the open market from shareholders at such price not exceeding the then market price as the trustees in the exercise of an absolute discretion may determine and agree upon, one or more preferred shares or one or more common shares from the holders thereof upon such terms and conditions of sale and purchase as may be agreed upon by the trustees in the exercise of their sound discretion, and to that end and for that purpose may use any of the surplus or surplus profits or capital assets of the trust in cash or otherwise for the payment of the purchase price on such shares so purchased, provided, however, that in no

case shall any purchase price paid per share be greater than the then net book value per share, and any and all shares so purchased by the trustees may in the exercise of their absolute discretion be cancelled or held in the treasury of the trust as an asset and part of the trust estate, and thereafter sold, used as collateral or in any other manner that other assets in the hands of said trustees may be used hereunder, and if cancelled the same may nevertheless be subsequently reissued and resold at any time by the trustees.

28. The trustees may at any time and from time to time hereafter sell, pledge or otherwise dispose of any and all of said preferred shares and any and all of said common shares at such price or for such purpose and upon such terms and conditions as the said trustees in the exercise of their absolute discretion may determine and decide upon.

29. As evidence of the ownership of the said shares the trustees shall cause to be issued and delivered to all purchasers or transferees thereof a negotiable certificate or certificates which shall be in such form and contain such matters and things as the trustees in the exercise of their absolute discretion shall determine and decide upon.

30. The trustees may at any time and from time to time distribute to the beneficiaries such income, proceeds or other parts of the trust estate as they may determine. All distribution of the income, proceeds or other parts of the trust estate, and the amount and conditions of payment and distribution thereof among the beneficiaries, except as to the preferred shares, the dividends on which shall be

paid as hereinbefore provided for, and except in case of the termination [16] of this trust, shall rest in the absolute discretion of the trustees, whose decision with respect thereto shall be final. The trustees may retain, undistributed, such sums as they may deem wise to create a sinking, reserve, surplus or contingent fund, provided, however, that no distribution of capital assets as distinguished from surplus or surplus profits shall be made prior to the final winding up of the affairs of the trust as a whole, unless and except in the case of the purchase by the trustees of any then outstanding preferred shares or common shares as hereinbefore provided, and the payment of the purchase price therefor.

31. In case of the loss or destruction of any certificate of shares, the trustees may, under such conditions as they may deem expedient, issue a new certificate or certificates in place of those lost or destroyed.

32. Shares hereunder shall be personal property only and give only the rights in this instrument specifically set forth.

33. The death, insolvency or incapacity of any shareholder during the continuance of this trust, or the levy upon or sale of any share under any attachment, execution, or other process of law whatever, shall not operate to terminate this trust, nor entitle the legal representatives or heirs or assigns or successors in interest, voluntary or involuntary, of such deceased, insolvent, or incapacitated or debtor shareholder to an accounting or distribution or to take any action, at law or in equity, or otherwise, in the courts or elsewhere, against the trustees, but such

legal representatives, heirs, assigns, or successors in interest shall succeed only to the rights of such deceased insolvent, incapacitated or debtor shareholder, subject to this Declaration of Trust, and shall succeed to nothing more.

34. The ownership of shares hereunder shall not entitle such owners to any title in or to the trust property whatsoever, or right to compel a partition or division of the same or an accounting, it being expressly declared that the said shareholders, otherwise sometimes referred to herein as beneficiaries, are cestuis que trustent, and hold no other relation to the trustees than that of cestuis que trustent hereunder. The shareholders shall only have the rights specifically set forth in this instrument, that is to say, the right to dividends, only as the same shall be declared by the trustees, and in case of the liquidation of all assets of the trust the proceeds, after the payment of all debts and liabilities of the trust, shall be divided amongst the shareholders in accordance with their respective priorities and in proportion to their respective holdings. [17]

35. Neither this declaration of trust nor the ownership of any of the shares issued hereunder shall constitute the parties hereto or their respective successors in interest or assigns, or any person who acts hereunder as trustee or who may become a beneficiary hereunder, as partners, nor to impose upon them or any of them any partnership or other liability similar to the liability of partners or any liability whatever other than the liability, if any, expressly imposed by this declaration, it

being expressly stipulated and declared and agreed by the trustees in the execution of this declaration and by the beneficiaries in the acceptance of the certificates evidencing their shares issued hereunder that a trust and not a partnership is hereby created, and that the appointment by the trustees of any directors or executive officers or of an executive committee or of an advisory board or of any other advisory officers is not intended to and shall not be held or construed to lessen the powers of the trustees hereunder, but that in any and every such case such appointment by the trustees shall be exclusively for advisory purposes only, and further that the power vested in the trustees to appoint such representatives or assistants may or may not be exercised by said trustees in their discretion.

36. The fiscal year of the trustees hereunder shall begin on the first day of January, beginning with the year 1922, and end on the 31st day of December in each year.

37. This trust shall continue for a term of twenty-five years from and after the date hereof or until it shall be sooner terminated by the trustees who are thereunto duly authorized and empowered in the exercise of their absolute discretion; upon the expiration of said term or the sooner termination of this trust, as aforesaid, by the trustees, the trustees shall proceed to wind up the affairs of the trust and distribute the assets thereof, or to sell the assets and distribute the proceeds thereof amongst the shareholders in accordance with their respective holdings, and in accordance with and subject to the respective

rights and priorities of the holders of the preferred shares and of the common shares as hereinbefore expressed.

38. Upon the termination of this trust, whether by limitation as above provided, or otherwise, and upon the liquidation of the trust estate, its proceeds shall be applied as follows, to wit:

First: To the payment of all prior costs, charges and expenses then remaining unpaid.

Second: To the payment of all indebtedness or obligations theretofore incurred by or on behalf of the trustees and then remaining unpaid. [18]

Third: To the payment of dividends and distribution of capital assets to the preferred shareholders and common shareholders in accordance with their respective holdings and in accordance with and subject to the respective rights and priorities as hereinbefore expressed.

39. A duplicate original of this declaration of trust shall be deposited with the Commissioner of Corporations of the State of California. In event of the abolition of the said office of Commissioner of Corporations said duplicate original of this declaration of trust and any other documents heretofore deposited or hereafter to be deposited with the Commissioner of Corporations hereunder, shall be deposited in the office required by law to take over and preserve the records and archives of said Commissioner of Corporations, if any, and if not the same shall in that event, but not otherwise, be deposited with such other depositary as the person

last occupying the office of Commissioner of Corporations shall designate, which depositary must be a responsible bank or trust company in the said City of Los Angeles; during the time that the said Declaration of Trust is in the possession of said last mentioned depositary it shall be permitted without further or other authority than that herein now granted, to permit the holder of any share issued hereunder to examine and inspect this Declaration of Trust, but not to remove the same from its office, the test of ownership in any case to be the production of a certificate evidencing such ownership, and such identifications as in the judgment of said depositary may be deemed necessary.

40. The trustees shall also deposit in the office of the Commissioner of Corporations of the State of California, such other and further documents and copies of documents of instruments as they may be lawfully required so to do by the Commissioner of Corporations of the State of California.

41. The trustees from time to time shall determine to what extent and at what times and places, and under what conditions and regulations the accounts, books and documents of the trustees, or any of them, shall be open to the inspection of the beneficiaries, and no shareholder shall have the right to such inspection except as authorized by the trustees.

42. If any person or persons holding in the aggregate twenty (20%) per cent of the outstanding beneficial shares of the trust estate, or twenty (20%) per cent of any class of such shares, shall

present to any officer or trustee of the trust estate a written request for a statement of its affairs, it shall be his duty to make or procure such statement sworn to by the President or the Vice-President, or by the Treasurer, [19] embracing a particular account of its assets and liabilities in detail, and to have the same ready and on file at the principal business office of the trustees within thirty (30) days after the presentation of such request, and such statement shall at all times during business hours be open to inspection of the holder of any beneficial shares, and he shall be entitled to copy the same.

43. Original or duplicate share ledgers containing the names and addresses of holders of the beneficial shares of this trust, and the number of shares of each class held by them, respectively, shall, during the usual business hours of every business day, be open for the inspection of any person or persons holding in the aggregate twenty (20) per cent of the outstanding beneficial shares, or of either class thereof, at the principal business office of the trustees; provided, however, that this provision shall be deemed complied with if the share ledger open for inspection as aforesaid discloses all transfers made up until twenty (20) days before such inspection. The other books of the trustees shall be open to inspection by holders of certificates for shares of beneficial interest upon the terms on which share ledgers are open to their inspection.

44. The trustees may at any time, and from time to time in their absolute discretion, make reports

in writing to the beneficiaries as to the condition, operation and management of the trust estate, or they may convene the holders of preferred beneficial interest shares and the holders of common beneficial interest shares in meeting to make oral or written reports to said beneficiaries, in reference to the administration of the trust and the condition of the trust property, to consider recommendations as to the filling of vacancies existing among the trustees, and for any other purpose which the trustees may determine. The said meeing shall be held at such time and place, and under such conditions and upon such notice as the trustees may determine. At any such meetings, where an advisory vote of the beneficiaries is desired by the trustees, each beneficiary may vote in person, by proxy, or in writing, under such terms and conditions as the trustees may provide. The trustees, however, shall not be bound by any such recommendations or suggestions or by any advisory or other vote of the beneficiaries, nor to act in accordance therewith, but may disregard the same in whole or in part.

45. This agreement and Declaration of Trust may be amended or altered by the trustees in any particular whatsoever, except as regards the exemption from personal liability of the trustees, beneficiaries, executive committee, officers, repre- [20] sentatives, agents, and employees, the priority of preferred beneficial interest shares and the acquired rights of third persons, and except as regards the limitations upon the right of the trustees to increase

the number of preferred shares issuable hereunder or to issue any other shares having any preference or priority over the preferred shares authorized hereunder, and also except as to the provisions hereunder prohibiting the Trustees from distributing capital assets as distinguished from surplus profits prior to the liquidation of the affairs of the trust as a whole, other than in connection with the purchase by the trustees of any shares and except as regards the provisions hereof prohibiting the trustees from levying or collecting assessments upon preferred shares. In the event any such alteration or amendment is made by the trustees the same shall be executed in like manner as this declaration is executed, and attached *to made* a part of this declaration and a copy thereof likewise executed and deposited with the Commissioner of Corporations of the State of California. Nothing in this paragraph contained shall in any way be construed to limit the power of the trustees to increase the number of the common shares or to issue shares junior in right to the preferred shares hereinbefore authorized, and having preference over the common shares.

46. This instrument is executed and delivered by the trustees in the State of California, and with reference to the laws thereof, particularly to the provisions of Sections 857 and 2220 of the Civil Code of said State, and the rights of all parties and the construction and effect of each and every provision hereof shall be subject to, and construed, according to the laws of said State.

47. In the construction of these presents words in the singular number include the plural number and vice versa, and words denoting males include females, and words denoting persons include firms, associations, trusts and corporations, and the word trustees shall extend to and include the trustees for the time being of these presents, and the words beneficiary and shareholders are used synonymously with each other, unless in any of said cases a contrary intention is clearly inferred from the subject matter or context.

IN WITNESS WHEREOF the said trustees have hereunto set their hands and seals to this instrument and to two other instruments of like tenor in token of their acceptance and declaration of the trust hereinbefore set forth on this the 25th day of September in the year of our Lord nineteen hundred and twenty-one.

(Signed) T. A. MORRISSEY [Seal]
(Signed) JAMES M. O'BRIEN [Seal] [21]

State of California,
County of Los Angeles—ss.

On this 4th day of October, 1921, before me, IDA M. DASKAM, a Notary Public in and for the said County of Los Angeles, State of California, residing therein, duly commissioned and sworn, personally appeared T. A. MORRISSEY and JAMES M. O'BRIEN, personally known to me to be persons whose names are subscribed to the within instru-

ment, and acknowledged to me that they executed the same.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal in said county the day and year in this certificate first above written.

[Notarial Seal] (Signed) IDA M. DASKAM, Notary Public in and for the County of Los Angeles, State of California. [22]

United States Board of Tax Appeals

Docket No. 40977.

T. A. MORRISSEY and JAMES M. O'BRIEN, Trustees of an Express Trust, known as Western Avenue Golf Club,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

STIPULATION FOR SUPPLEMENTAL TRANSCRIPT.

The petitioners in the above entitled cause having filed a petition for review of the decision of the United States Board of Tax Appeals by the Circuit Court of Appeals for the Ninth Circuit, and the petitioners having in the praecipe for the record requested that the stipulation of facts be trans-

mitted to the United States Circuit Court of Appeals for the Ninth Circuit, which stipulation of facts referred to and incorporated a certain declaration of trust as exhibit "B" but which declaration of trust was not attached thereto and was not transmitted to the Circuit Court of Appeals for the Ninth Circuit but which should be transmitted, counsel for petitioners and counsel for respondent do hereby stipulate and agree that the Clerk of the United States Board of Tax Appeals may cause to be prepared, certified and transmitted to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit a supplemental transcript of the record of the above entitled [23] cause, which supplemental transcript shall contain the following: Exhibit "B" referred to and incorporated in paragraph two of the stipulation of facts, which said Exhibit "B" is a declaration of trust by T. A. Morrissey and James M. O'Brien dated October 4, 1921.

Counsel further stipulate that the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit shall add to the record the said Exhibit "B" and make the same a part thereof.

THEODORE B. BENSON,
917 Southern Building,
Washington, D. C.,
Counsel for Petitioners.

FRANK J. WIDEMAN,
Assistant Attorney General.

[Endorsed]: U. S. Board of Tax Appeals. Filed Jan. 9, 1934. [24]

[Title of Court and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 24, inclusive, contain and are a true copy of the supplemental transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 13th day of June, 1934.

[Seal] B. D. GAMBLE,
Clerk, United States Board of Tax Appeals. [25]

[Endorsed]: No. 7364. United States Circuit Court of Appeals for the Ninth Circuit. T. A. Morrissey and James M. O'Brien, Trustees of an Express Trust, known as Western Avenue Golf Club, Petitioners, vs. Commissioner of Internal Revenue, Respondent. Supplemental Transcript of the Record. Upon Petition to Review an Order of the United States Board of Tax Appeals.

Filed July 2, 1934.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals for the Ninth Circuit.

SUPREME COURT OF THE UNITED STATES

ORDER ALLOWING CERTIORARI—Filed May 13, 1935

The petition herein for a writ of certiorari to the United States Circuit Court of Appeals for the Ninth Circuit is granted. And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.

FILE COPY

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FILED
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CHARLES ELMORE CROP

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934

No. [redacted] 17

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES OF AN EXPRESS TRUST, KNOWN AS WESTERN AVENUE GOLF CLUB,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

THEODORE B. BENSON,
Counsel for Petitioners.

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SUPREME COURT OF THE UNITED STATES
OCTOBER TERM, 1934

No. 834

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES OF AN EXPRESS TRUST, KNOWN AS WESTERN AVENUE GOLF CLUB,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT AND BRIEF IN SUPPORT THEREOF.

Petition.

Theodore B. Benson, on behalf of T. A. Morrissey and James M. O'Brien, trustees of an express trust, known as Western Avenue Golf Club, prays that a writ of certiorari be issued to review the judgment of the United States Circuit Court of Appeals for the Ninth Circuit entered January 7, 1935 (R. 67), affirming a memorandum decision of the United States Board of Tax Appeals (R. 30-51), petition for rehearing having been filed February 5, 1935, and denied March 1, 1935 (R. 74).

A.

Summary Statement of the Matter Involved.

The matter involved is the meaning of the word "association" in Section 2 of the Revenue Acts of 1924 and 1926,

43 Stat. 253, 44 Stat. 9, in determining whether the petitioners should be taxed as a corporation under Part II or as a trust under Part I of the Acts.

On October 4, 1921, T. A. Morrissey and James M. O'Brien executed a declaration of trust (Supplemental R. 1-38), to a certain tract of land in the City of Los Angeles consisting of 155 acres, about 42 acres of which were surveyed into lots and sold during 1921 and 1922 through a broker and his salesmen (R. 24). The sales were on the installment basis and collections were made by an agent bank.

On the remainder of the tract the trustees in 1922 constructed a golf club which they operated until January 12, 1924 (R. 26-28).

During the years here in controversy and except for the 12 days in 1924 the only activities of the trust were: (1) Receipt from agent bank of principal and interest collected on installment sales contracts; (2) receipt of credit of interest earned on bank balances; (3) receipt of assignment fees from holders of lot purchase contracts; (4) conveyance of lots to purchasers thereof; (5) receipt of dividends from Western Avenue Golf Club, Inc., upon shares thereof owned by petitioners; (6) distribution of moneys to holders of beneficial interests in the trust by way of dividends and, in some cases, by way of redemption and retirement of beneficial interests (R. 28, 29).

During the years 1924, 1925 and 1926 the outstanding shares ranged from 2,172 to 2,897 and the number held by the two trustees ranged from 451 and a fraction to 632 and a fraction (R. 30). The approximate number of holders of beneficial interest ranged from 275 to 675 (R. 31).

T. A. Morrissey and James M. O'Brien have ever since continued to be and now are the sole trustees (R. 29). The holders of beneficial interest had no voice in the management or administration of the trust, no power to remove

trustees nor to elect their successors nor to control their actions, nor even the right to inspect the books (Supplemental R. 2, 3).

The petitioners filed returns as a trust for each of the years in question (R. 23). The Commissioner of Internal Revenue determined that the trust constitutes an association and assessed a deficiency for each of the years at the rates prescribed for a corporation (R. 13). The Board of Tax Appeals sustained the Commissioner and a petition for review was filed with the Circuit Court of Appeals for the Ninth Circuit and that court affirmed the decision of the Board (R. 67).

B.

Reasons for the Allowance of the Writ.

The Circuit Court of Appeals for the Ninth Circuit has decided an important question, the definition of the word "associations", as to which, as pointed out in *Coleman-Gilbert Associates* v. *Commissioner*, decided February 27, 1935, by the First Circuit, no absolute, conclusive or definite test has been prescribed by this Court, although a statute involving similar provisions was considered by this Court in *Crocker* v. *Malley*, 249 U. S. 223, and the provisions of an excise tax law were considered by this Court in *Hecht* v. *Malley*, 265 U. S. 144.

The question in this case should be passed on by this Court and the court below should be reversed for the following reasons:

"1. The decision of the court below is in direct conflict with the decision of this Court in *Crocker* v. *Malley, supra*, and with the most recent decision on the question that by the United States Circuit Court of Appeals for the First Circuit in *Coleman-Gilbert Associates* v. *Commissioner*, 1935 C. C. H., Volume III, page 9589, in which the Commissioner of Internal Revenue will doubtless apply for a writ of certiorari.

2. The only decision of this Court on the question here involved is that in *Crocker* v. *Malley, supra.* The parties to *Crocker* v. *Malley* were parties to a case that was later before this Court and reported as *Hecht* v. *Malley, supra,* but in the meantime the powers of the trust had been enlarged and it was functioning as an ordinary corporation and, further, the same tax was not involved nor was the same question before the Court. There is no statement in the opinion in the later case that the decision in the former is modified nor in any way departed from.

3. The court below erred in applying as the test to distinguish an association from a pure trust merely the so-called "business test" and gave no consideration to test of function in a corporate manner.

4. In applying as the sole test to distinguish an association from a pure trust, that of doing business, the court below erred in merely following the provisions of the trust and gave no consideration to the activities actually engaged in by the trustees. In this application of the "business test" the decision of the court below is in direct conflict with the decision of the First Circuit in the case of *Coleman-Gilbert Associates* v. *Commissioner, supra,* and the decision gives no consideration to the changed state of facts that was presented to this Court when the *Crocker* case came up a second time in *Hecht* v. *Malley, supra.*

WHEREFORE your petitioners respectfully pray that a writ of certiorari be issued to review the judgment of the Circuit Court of Appeals for the Ninth Circuit, and that the judgment of that court be reversed by this Honorable Court.

THEODORE B. BENSCOTER,
1127 *Munsey Building, Washington, D. C.,*
Counsel for Petitioners.

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1934

No. 834

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES OF AN EXPRESS TRUST, KNOWN AS WESTERN AVENUE GOLF CLUB,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI.

I.

The Opinion of the Court Below.

The opinion in the Circuit Court of Appeals for the Ninth Circuit was handed down on January 7, 1935, reported in 74 F. (2d) 803, and an order denying petition for rehearing was entered March 1, 1935.

II.

Jurisdiction.

The jurisdiction of this Court is invoked under the Judicial Code, Section 240, as amended by the Act of February

13, 1925, 43 Stat. 938, and Section 1003 (a) of the Revenue Act of 1926, 44 Stat. 110.

The date of the judgment to be reviewed is January 5, 1935. Application for the writ was presented April 1, 1935.

III.

The Facts.

The facts appear in the record (R. 22-31) and in the supplemental transcript of record. A summary statement of the facts is printed in the petition for the writ and to avoid repetition counsel begs leave to refer thereto. The statement in the petition is the shortest and plainest he has been able to make.

IV.

The Statutes Involved.

The provisions of the Revenue Acts of 1924 and 1926 here pertinent are contained in Section 2, in which a corporation is defined to include an association, and in Section 219, in which provision is made for taxing a trust as an individual. Section 2 (a) 2 of each Act reads as follows:

> "The term 'corporation' includes associations, joint stock companies and insurance companies."

Section 219 of the Revenue Act of 1924 and 1926 which relates to trusts provides for the imposition of the individual income tax on either the trustee or the beneficiary.

V.

Specifications of Error.

The United States Circuit Court of Appeals for the Ninth Circuit erred in holding that the trust constitutes an association which should be taxed as a corporation and not a

pure trust which should be taxed at the rates prescribed for individuals.

VI.

THE ARGUMENT.

The Question Is One of Importance.

That the question here involved is one of importance counsel for petitioners feels need not be supported by argument. Counsel for respondent will doubtless concede this but may contend that the question has been put at rest.

The Question Should be Passed On by This Court.

The exact question here involved, the definition of the word "associations" for the purposes of the imposition of the income tax was before this Court in the case of *Crocker* v. *Malley, supra,* and by the application of the test of functioning in a corporate manner this Court held, on a state of facts similar to those involved in the instant case, that the trust should not be taxed as a corporation but as a pure trust. Under a changed state of facts which evidenced that the trust was engaged in doing business in a corporate manner this Court, in *Hecht* v. *Malley, supra,* considered the definition of the word "associations" for the purposes of imposing an excise tax on the privilege of doing business and held that the trust, under the changed state of facts, constituted a corporation and not a pure trust.

Following the decisions in the cases of *Crocker* v. *Malley* and *Hecht* v. *Malley, supra,* the Treasury Department has promulgated various rulings and has changed its position, as pointed out by the court below, which rulings have, however, not been definite nor consistent, as pointed out by the Circuit Court of Appeals for the First Circuit in the case of *Coleman-Gilbert Associates* v. *Commissioner, supra.*

Despite the decision of this Court in *Crocker* v. *Malley, supra,* the question here involved remains one of doubt as discussed below.

Conflict of Decisions.

While the question may have heretofore been before this Court and was decided favorably to the petitioners, the decisions of the lower courts are at this time conflicting and the court below rendered a decision contrary to that of this Court in *Crocker* v. *Malley, supra.*

The court below disregarded entirely the corporate function test and applied what it termed the business test. With reference to this the court stated:

> "As to the contention that 'doing business' is not controlling or relevant, this court in *Twin Bell Oil Syndicate* v. *Helvering,* 70 F. (2d) 402 (C. C. A. 9), after quoting from its opinion in the Trust No. 5833, *Security First National Bank* v. *Welch,* 54 F. (2d) 323 (C. C. A. 9), said at page 407:
>
> 'There is ample additional authority for the proposition that the 'business' test is now paramount.' "

In applying the business test the court based its decision on the business activities authorized by the declaration of trust and did not give consideration to the business activities actually engaged in. In this connection the attention of this Court is invited to the fact that, except for a period of 12 days, the business activities were confined to the collection of outstanding payments on contracts previously entered into for the sale of lots, completing the transfer of title to lands sold and the receipt and distribution of income. These activities are not comparable to doing business as is ordinarily done by a corporation, but were in fact merely steps to the liquidation and termination of the trust. In the respondent's brief in the court below it is

conceded that had the petitioner been a liquidating trust it would not have been taxable as a corporation. The petitioners submit that the trust should be considered as in process of liquidation rather than engaged in the conduct of business as an ordinary corporation.

The court below simply followed its prior decisions and made no attempt to discuss or reconcile the decisions in other circuits, as is very ably done by Judge Wilson of the First Circuit in *Coleman-Gilbert Associates* v. *Commissioner, supra,* in which a trust engaged in more activities than the trust in the instant case was classified as a pure trust and not as an association.

In the case of *Coleman-Gilbert Associates, supra,* the unsettled meaning of the word "associations" is clearly pointed out and the conflicting decisions are cited and the petitioners respectfully submit that the opinion therein clearly indicates that the writ should be granted in this case. The court there reviews the decisions of this Court in the cases of *Crocker* v. *Malley* and *Hecht* v. *Malley, supra,* and with reference to the latter case states (italics supplied:

> "Congress has not undertaken to lay down any tests for determining whether an organization is an association • • •.
>
> It was left for the courts or the Treasury Department by Regulations to determine what organizations are included within the term "associations." *As yet the Supreme Court has not laid down any absolute test.* Two cases only have come before it in which the taxing of trusts as associations was involved: *Crocker et al., Trustees,* v. *Malley,* 249 U. S. 223; *Hecht et al., Trustees,* v. *Malley,* 265 U. S. 144.
>
> This appears to be the last word of the Supreme Court that is helpful in determining what is included in the term "association."
>
> *The Treasury Department has endeavored from time to time to clarify the situation by Regulations* defining

associations and trusts. Under Art. 1504 of Regulation 62, it followed what it understood was the holding of the court in *Crocker* v. *Malley, supra,* and provided that /.

Where trustees hold real estate subject to a lease and collect the rents, doing no business other than distributing the income less taxes and similar expenses to the holders of their receipt certificates, who have no control except the right of filling a vacancy among trustees and of consenting to a modification of the terms of the trust, no association exists. • • • If, however, the *cestuis qui* trust have a voice in the conduct of the business of the trust, whether through the right periodically to elect trustees or otherwise, the trust is an association. • • •

In 1926, following the decision in the *Hecht* v. *Malley* case, by Regulation 69, Arts. 1502 and 1504, and again in 1928, by Regulation 74, Arts. 1312 and 1314, it was provided that, in addition to the above tests in Regulation 62, "if, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists. • • • Even in the absence of control by the beneficiaries where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors of a corporation for the purpose of carrying some business enterprise, the trust is an association within the meaning of the statute."

There are numerous decisions of the Board of Tax Appeals and Circuit Courts of Appeals in review, without laying down any definite line of demarkation between an association and a pure trust. In some instances the courts have based their decisions on the rule that where the administrative board has construed an ambiguous or indefinite definition in a statute and no change was made in a later Act of Congress, it is presumed that Congress had adopted the definition

adopted by the administrative board; in other cases the courts have been influenced by other considerations: the limited activities of the trustees, and the purpose of the trust. In any event, the decisions are seemingly in a hopeless state of confusion. Klein's Federal Income Taxation, p. 1139, para. 34:9, and 1933 Suppl., para. 34:9. As the Regulations of the Treasury Department have been modified from time to time, it may well be questioned whether Congress has intentionally adopted every modification of the Regulations when it makes no change in the language of its Acts; or whether it has left it for further construction by the courts, especially if the Regulations have not followed closely the language of the courts. *Tyson et al.* v. *Commissioner*, 68 F. (2d) 584; Trust No. 5833, *Security-First Nat. Bank of Los Angeles* v. *Welch*, 54 F. (2d) 323, 326.

It would serve no useful purpose to attempt to analyze all the cases that have been decided by the Board of Tax Appeals and the Circuit Courts of Appeals involving this question. *The lack of a conclusive test will sufficiently appear in the following cases in which the Board of Tax Appeals has been sustained in holding a trust was an association: Willis et al.* v. *Commissioner*, 58 Fed. (2d) 121; *Smith* v. *Commissioner*, 69 Fed. (2d) 911; *Little Four Oil & Gas Co.* v. *Lewellyn*, 35 Fed. (2d) 149; Trust No. 5833, *Security-First Nat. Bank of Los Angeles* v. *Welch, supra; Sloan et al.* v. *Commissioner*, 63 Fed. (2d) 667; *Investment Trust of Mutual Investment Co., Empire Trust Co., Trustee,* v. *Commissioner*, 71 Fed. (2d) 1009; and in the following cases in which the court has either reversed the Board in holding that the trust was an association, or has approved the Board's finding that the trust was not an association: *Landsdowne Realty Trust* v. *Commissioner*, 50 Fed. (2d) 56; *Lucas, Commissioner,* v. *Extension Oil Co.*, 47 Fed. (2d) 65; *Commissioner* v. *Morris Realty Co. Trust*, 68 Fed. (2d) 648; *Commissioner* v. *Pryor & Lockhart Development Co.*, 70 Fed. (2d)

154, 158; *Commissioner* v. *Kelley* et al., Trustees (decided Dec. 4, 1934 (C. C. A.)).''

In Rewrite Federal Tax Service for 1935, page 1040, paragraph 64, published by Commerce Clearing House, it is stated with reference to the questions here involved:

> ''In spite of much litigation on this question the last word has not yet been spoken as to where the line is to be drawn between a pure trust and an association.''

The conflict here presented is not one arising from different facts, but from the uncertainty as to the tests to be applied.

Conclusion.

In view of the facts that the decision below is in direct conflict with the decision of this Court in *Crocker* v. *Malley, supra,* and with the decision of the Circuit Court of Appeals for the First Circuit in *Coleman-Gilbert Associates* v. *Commissioner, supra,* and that there is confusion as to the definition of the word ''associations'' and as to the tests to be applied to determine when a trust should be taxed as a corporation, the petitioners submit that the writ should be granted and that the holding of the court below that the business test alone is sufficient to cause a trust to be taxed as a corporation, should be reversed.

THEODORE B. BENSON,
1127 *Munsey Building,*
Washington, D. C.,
Counsel for Petitioners.

(6171-C)

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1935.

No. 17.

T. A. MORRISSEY AND JAMES M. O'BRIEN, Trustees of an Express Trust, Known as Western Avenue Golf Club,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF FOR PETITIONERS.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT.

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Washington, D. C.

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Roanoke, Virginia.

ALEXANDRIA PRINT SHOP, INC., ALEXANDRIA, VIRGINIA

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1935.

No. 17.

T. A. MORRISSEY AND JAMES M. O'BRIEN, Trustees of an Express Trust, Known as Western Avenue Golf Club,

Petitioners,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

BRIEF FOR PETITIONERS.

STATEMENT OF THE CASE

This case is before this Court on a writ of certiorari to review a decision of the United States Circuit Court of Appeals for the Ninth Circuit, affirming a decision of the United States Board of Tax Appeals redetermining deficiencies in corporation income tax for the calendar years 1924, 1925 and 1926 in the amounts of $1,890.55, $1,623.49 and $1,036.90.

The petitioners filed income tax returns as trustees as required by Section 219 of the Revenue Act of 1924 (43 Stat. 275), and of the Revenue Act of 1926 (44 Stat. 32). The Commissioner of Internal Revenue determined that the trust constituted an association within the meaning of Section 2 of

the Revenue Act of 1924 (43 Stat. 253), and the Revenue Act of 1926 (44 Stat. 9), and that the petitioners should be taxed at the corporation rate and deductions of amounts distributed to beneficiaries should be disallowed. An appeal was taken to the Board of Tax Appeals and the Commissioner was upheld in his determination that the trust was an association and on review to the United States Circuit Court of Appeals the decision of the Board was affirmed.

This Court granted the writ of certiorari May 13, 1935, to review the decision of the court below.

I.

Opinion of the Court Below.

The opinion of the court below was rendered on January 7, 1935. The opinion has been reported in 74 Fed. (2d) 803 and is a part of the record on this appeal (R. 67-72).

II.

Jurisdiction.

This Court has heretofore granted a writ of certiorari under the Judicial Code, Section 240, as amended by the Act of February 13, 1925 (43 Stat. 938), and Section 1003 (a) of the Revenue Act of 1926 (44 Stat. 110) as amended by Section 603 of the Revenue Act of 1928 (45 Stat. 873) and Section 1101 (a) of the Revenue Act of 1932 (47 Stat. 286) (26 USCA 1224-1226).

III.

Specification of Error

The court below erred in holding that the trustees should be taxed as a corporation and not as a pure trust under Section 219 of the Revenue Acts of 1924 and 1926.

IV.

THE FACTS.

The taxable entity, whether a pure trust or an association, was created October 4, 1921, by a document entitled "Western Avenue Golf Club Declaration of Trust" in which T. A. Morrissey and James M. O'Brien of Los Angeles, California, declared themselves trustees to hold a certain tract of land previously conveyed to them and also any other property to be conveyed to them on terms and conditions stated in the declaration of trust. The declaration of trust is printed in full in the supplemental transcript of record.

The declaration of trust provides that the trustees shall be designated and act in their collective capacity as Western Avenue Golf Club; and that additional trustees shall be selected and vacancies shall be filled by the trustees designated in the instrument and their successors. The two original trustees have acted continuously since the creation of the trust and no additional trustees have been appointed and there have been no vacancies (R. 29).

The powers conferred on the trustees are the usual powers to purchase, hold, improve and manage property. The trustees have authority to adopt rules and regulations, to adopt and use a common seal, to remove trustees (except the original trustees) officers or members of any committee, to appoint an advisory board to be known as directors, to appoint an executive committee, to remove members of advisory board or executive committee or holders of other offices. The instrument provides that the trustees may and the directors and executive committee shall hold meetings in such manner and at such times as the trustees may determine.

The trustees have no power to bind the beneficiaries personally and neither the death of a trustee nor of a beneficiary shall terminate the trust.

The declaration of trust provides that the beneficial shares shall be divided into 2,000 preferred shares of the par value of $100.00, and the common shares of no par value. The preferred shares shall be nonassessable but assessments may be levied on the common shares when deemed necessary or advisable by the trustees.

The instrument expressly provides that the ownership of shares shall not entitle the beneficiary to the right to compel partition and further that neither the declaration of trust nor the ownership of shares shall constitute the parties partners.

The trust is declared to continue for a term of 25 years unless sooner terminated by the trustees.

Provisions are made for the maintenance of books, the amendment of the declaration of trust by the trustees and for the deposit of a duplicate original with the Commissioner of Corporations of the State of California, Sections 857 and 222 of the Civil Code of which State are therein referred to and the provision is made that the rights of all parties and the construction and effect of each and every provision thereof shall be subject to, and construed, according to the laws of that State.

The tract of land which had been previously conveyed to the trustees consisted of 150 acres, 42 acres of which were surveyed and plotted into lots which, beginning December 20, 1921, were sold through a broker. This subdivided property was improved by the construction of streets, sidewalks, and curbs during the year 1922. All of the lots in the 42 acres were sold by the end of 1923. Most of the sales were on installment basis and collections on the sales contracts were made through the collection department of a bank (R. 26, 28).

On the remaining 113 acres, which were not subdivided, a golf course was constructed and completed in September, 1922.

and a club house connected with it was completed in December, 1922.

In July, 1923, the 113 acres comprising the golf course, together with all improvements and equipment, were sold and conveyed to Western Avenue Golf Club, Inc., a California corporation, in exchange for its stock and without other consideration. During the years 1924 and 1925 and 1926, the petitioners received dividends from the said corporation on the stock so acquired in the amounts of $53,560.65, $21,973.60 and $21,973.60.

The petitioners, under a lease from the corporation, continued the operation of the golf course until January 12, 1924. The gross receipts from operations during the 12 days amounted to less than $400.00.

No activities have been engaged in by petitioner between December 31, 1923, and January 1, 1927, except: (1) operation of said golf course for the first 12 days of 1924 as aforesaid, (2) Receipt from collection agent bank of principal and interest so collected by said bank in behalf of petitioner, (3) Receipt of credit of interest earned on bank balances, (4) Receipt of assignment fees in assignment of lot purchase contracts by holders thereof, (5) Conveyance of lots to purchasers thereof, (6) Receipt of dividends from Western Avenue Golf Club, Inc., upon shares thereof owned by petitioner, (7) Distribution of moneys to the holders of beneficial interests in petitioner trust by way of dividends and, in some cases, by way of redemption and retirement of their beneficial interests (R. 28).

The number of beneficial interests issued by the trustees and outstanding during the years in question appear on page 30 of the Transcript of Record. On December 31, 1923, the total number of interests outstanding was 3,016. By December 31, 1926, the interests had gradually decreased to 2,172. The holdings of the trustees ranged from approximately 16 per

cent. to 29 per cent. The number of persons holding beneficial interests on December 31, 1923, was 920, and the number had reduced to 275 by December 31, 1926.

The trustees filed returns and paid the tax at the individual rates.

In the returns the petitioners included in income the dividends received from Western Avenue Golf Club, Inc., and deducted distributions to beneficiaries of the trust in the amounts of $56,829.77, $20,648.00 and $17,511.10 (R. 26).

The respondent determined that the declaration of trust created an association taxable as a corporation, eliminated from income the dividends received from Western Avenue Golf Club, Inc., and denied the deduction of amounts distributed to beneficiaries. An appeal was taken from the deficiencies determined by the respondent to the United States Board of Tax Appeals which held that the trust should be taxed as an association. Review was sought in the Circuit Court of Appeals for the Ninth Circuit which affirmed the decision of the United States Board of Tax Appeals and followed its prior decision in the *Twin Bell Oil Syndicate*, 70 Fed. (2d) 402, which in turn had followed *Security National Bank* v. *Welch*, 54 Fed. (2d) 323, decided by the same court.

V.

THE STATUTES.

Section 219 of the Revenue Acts of 1924 (43 Stat. 275) and 1926 (44 Stat. 32) entitled "Estates and Trusts" provides that the tax imposed on individuals shall apply to the income of property held in trust. Subsection (b) provides that the net income of the trust shall be computed in the same manner as provided in Section 212, with certain exceptions, one of which is that there shall be allowed as a deduction distributions to beneficiaries. Section 219 is in part as follows:

(a) The tax imposed by Parts I and II of this title shall apply to the income of estates or of any kind of property held in trust, including—

* * * * * *

(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) * * * the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in Section 212, except that—

* * * * * *

(2) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. * * *

(3) * * * in the case of income which, in the discretion of the fiduciary, may be either distributed to the beneficiary or accumulated, there shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is properly paid or credited during such year to any legatee, heir, or beneficiary, but the amount so allowed as a deduction shall be included in computing the net income of the legatee, heir, or beneficiary. * * *

Section 2(a) of the Revenue Act of 1924 (43 Stat. 253) and of the Revenue Act of 1926 (44 Stat. 9) reads in part:

2(a) When used in this Act * * * (2) the term "corporation" includes associations, joint-stock companies, and insurance companies.

Section 704 of the Revenue Act of 1928, (45 Stat. 830) reads:

> (a) If a taxpayer filed a return as a trust for any taxable year prior to the taxable year 1925 such taxpayer shall be taxable as a trust for such year and not as a corporation, if such taxpayer was considered to be taxable as a trust and not as a corporation either (1) under the regulations in force at the time the return was made or at the time of the termination of its existence, or (2) under any ruling of the Commissioner or any duly authorized officer of the Bureau of Internal Revenue applicable to any of such years, and interpretative of any provision of the Revenue Act of 1918, 1921 or 1924, which had not been reversed or revoked prior to the time the return was made, or under any such ruling made after the return was filed which had not been reversed or revoked prior to the time of the termination of the taxpayer's existence.
>
> (b) For the purpose of the Revenue Act of 1926 and prior Revenue Acts, a trust shall, at the option of the trustee exercised within one year after the enactment of this Act, be considered as a trust the income of which is taxable (whether distributed or not) to the beneficiaries, and not as an association; if such trust (1) had a single trustee, and (2) was created and operated for the sole purpose of liquidating real property as a single venture (with such powers of administration as are incidental thereto, including the acquisition, improvement, conservation, division, and sale of such property), distributing the proceeds therefrom in due course to or for the benefit of the beneficiaries, and discharging indebtedness secured by the trust property, and (3) has not made a return for the taxable year as an association.

VI.

THE REGULATIONS.

The years here involved are 1924, 1925 and 1926 for the enforcement of which Treasury Department Regulations 65

and 69 were promulgated. However the statutory provisions relating to and distinguishing associations and trusts are the the same in all acts beginning with that of 1918 and the question arises whether the regulations have the effect of law. It is therefore in order to refer to the pertinent provisions of prior regulations. Article 1502 of Regulations 45 promulgated for the enforcement of the Revenue Act of 1918 (40 Stat. 1057) is:

> Associations and joint-stock companies include associations, common law trusts, and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the members or shareholders on the basis of the capital stock which each holds or, where there is no capital stock, on the basis of the proportionate share or capital which each has or has invested in the business or property of the organization.

The above provision was printed without change in Article 1502 of Regulations 62 for the enforcement of the Revenue Act of 1921 (42 Stat. 222) and Regulations 65 for the enforcement of the Revenue Act of 1924 (43 Stat. 253). These Regulations, 62 and 65, do however contain the following additional sentence:

> A corporation which has ceased to exist in contemplation of law but continues its business in corporate form is an association or corporation within the meaning of Section 2, but if it continues its business in the form of a trust, it becomes subject to the provisions of section 219.

Article 1504 of Regulations 45, reprinted without change as Article 1504 of Regulations 62, is:

> Where trustees hold real estate subject to a lease and collect the rents, doing no business other than distributing the income less taxes and similar expenses to the holders

of their receipt certificates, who have no control except the right of filling a vacancy among the trustees and of consenting to a modification of the terms of the trust, no association exists and the cestuis que trust are liable to tax as beneficiaries of a trust the income of which is to be distributed periodically, whether or not at regular intervals. But in such a trust if the trustees pursuant to the terms thereof have the right to hold the income for future distribution, the net income is taxed to the trustees instead of to the beneficiaries. See Section 219 of the Statute and Articles 341-347. If, however, the cestuis que trust have a voice in the conduct of the business of the trust, whether through the right periodically to elect trustees or otherwise, the trust is an association within the meaning of the Statute.

On June 7, 1924, subsequent to the Revenue Act of June 2, 1924; the Secretary of the Treasury approved and promulgated Treasury Decision 3598 which was first published June 16, 1924:

"To Collectors of Internal Revenue and others concerned:

In order to give effect to the decision of May 12, 1924, by the United States Supreme Court in the case of *Hecht* v. *Malley* and in the other cases named therein (Nos. 99, 100, 101, and 119—October Term, 1923), Article 7 of Regulations 50 (revised edition, approved June 21, 1920) and Article 8 of Regulations 64 are amended so as to read as follows:

Trusts.—Two distinct classes of trusts are recognized by the Department, namely, holding trusts and operating trusts.

Holding trusts are those in which the trustees are merely holding property for the collection of the income and distributing it among the beneficiaries and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business. Such

trusts are not associations within the meaning of the law and are not subject to the tax.

Operating trusts are those in which the trustees are not restricted to the mere collection of funds and paying them over to the beneficiaries but are associated together in much the same manner as directors in a corporation for the purpose of, and are actually engaged in, carrying on some business enterprise. These trusts, whether of the Massachusetts type or otherwise, are to be deemed associations within the meaning of the Act, independently of any control exercised by the beneficiaries, and subject to the tax."

In Regulations 65 promulgated October 6, 1924, Article 1504 originally read:

> Holding trusts, in which the trustees are merely holding property for the collection of the income and its distribution among the beneficiaries, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, are not associations within the meaning of the law. The trust and the beneficiaries thereof will be subject to tax as provided in articles 341-347. Operating trusts, whether or not of the Massachusetts type, in which the trustees are not restricted to the mere collection of funds and their payments to the beneficiaries, but are associated together in much the same manner as directors in a corporation for the purpose of carrying on some business enterprise, are to be deemed associations within the meaning of the Act, regardless of the control exercised by the beneficiaries.

By Treasury Decision 3749, C. B. IV-2 page 7, published August 31, 1925, Article 1502 of Regulations 65 was amended by causing the last sentence to read:

> A corporation which has ceased to exist in contemplation of law but continues its business in quasi corporate

form is an association or corporation within the meaning of Section 2.

By Treasury Decision 3748 published the same day, C. B. IV-2, page 7, Article 1504 was amended to read:

> Where trustees merely hold property for the collection of the income and its distribution among the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, and the beneficiaries have no control over the trust although their consent may be required for the filling of a vacancy among the trustees, or for a modification of the terms of the trust, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by section 219 and by articles 341-347. If, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists within the meaning of Section 2. Even in the absence of any control by the beneficiaries, where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the statute.

Articles 1502 and 1504 of Regulations 69 promulgated for the enforcement of the Revenue Act of 1926 are the same as Article 1502 and 1504 of Regulations 65 as amended.

Regulations 74 for the enforcement of the Revenue Act of 1928 contains no provision with reference to Section 704 of the Act.

VII.

THE ARGUMENT.

Summary of Argument.

A. In *Crocker* v. *Malley*, 249 U. S. 223, this Court had before it the case of a Massachusetts trust which was not

actively engaged in business and in which the beneficiaries were not associated together in the manner of a corporation and had no control over the trustees. In the case of *Hecht* v. *Malley*, 265 U. S. 144, this Court had before it the case of a Massachusetts trust actively engaged in business after the manner of a corporation and in which the beneficiaries had a voice in the management. In the instant case the trustees were not actively engaged in business after the form and manner of a corporation and the beneficiaries had no voice in the management. The case is therefore distinguishable from *Hecht* v. *Malley*.

B. The word "associations" does not necessarily have its ordinary meaning. The word as used in the Revenue Acts of 1924 and 1926 as well as the prior revenue acts, beginning with that of 1909 is grouped with the words "corporation", "joint-stock companies" and "insurance companies" and appears in entirely different provisions of the several acts from those relating to "estates" and "trusts". The rule of construction to be applied is therefore that the word "associations" includes only such associations as properly are comparable to corporations, joint-stock companies or insurance companies and is to exclude such taxpayers as properly are to be considered estates and trusts. The general rule of construction as applicable here that a word is presumed to have been used in its ordinary sense and meaning is therefore to be considered with and to be modified by the rule that a word is to be construed with reference to the context of the statute in which it appears.

C. The true test to be applied in classifying the trust as an association or as a pure trust is whether or not the trustees acted or carried on business after the form or manner of a corporation. This requires a quasi-corporate organization in which the beneficiaries, whether or not certificate holders, have some voice in the management and some control over the

trustees and have an opportunity to exercise such control through the right to vote at meetings.

D. Even if the so-called business test as applied by the Court below is the paramount test, the mere fact that the trustees under the declaration of trust do some business to the extent of retaining title to and collecting and distributing the income from the land and the shares of corporate stock placed in trust does not require that the trust be taxed as a corporation. In these meager activities the trustees were not acting or carrying on business as contemplated by this Court in *Hecht* v. *Malley*.

E. The activities actually engaged in by the trustees, rather than the possible activities authorized by the declaration of trust, are to be considered in determining whether or not they were acting or carrying on business in the form and manner of a corporation.

F. The provisions of the Revenue Act of 1924 are to be construed as adopting and approving the Treasury Department Regulations promulgated under previous laws and in force at the time of the enactment of the Revenue Act of 1924 and therefore the trustees are to be taxed as a pure trust for the year 1924 for the reason that under the adopted regulations they should not be considered an association. The regulations became law on the reenactment without change of the provisions of the previous statutes. The regulations had not been materially changed at the time of the enactment of the Revenue Act of 1926.

G. Pursuant to the retroactive provisions of Section 704 of the Revenue Act of 1928 the trustees are taxable as a trust because they filed a return as a trust and were considered to be taxable as a trust under regulations in force at the time the return was made. The section by its express terms embraces all years prior to 1925.

POINT A.

Hecht v. Malley is Distinguishable from Crocker v. Malley and the Instant Case.

In the case of *Crocker* v. *Malley*, 249 U. S. 223, this Court had before it the provision of the Act of October 3, 1913, (38 Stat. 177) which imposed a tax on the income of "every corporation, joint-stock company or association." The taxpayer was a real estate trust of the kind known as a "Massachusetts trust" in which the certificate holders were in no way associated together, no provision was made for meetings and they had no control over the trustees. In that case this Court held that the declaration of trusts did not create an association within the meaning of the provision of the Act of 1913 imposing the tax on an association. The Act of October 3, 1913, levied a tax on incomes and in *Brushaber* v. *Union Pacific*, 240 U. S. 1, this Court held the act was constitutional as not repugnant to the Fifth Amendment and not inconsistent with the Sixteenth Amendment of the Constitution.

The petitioners submit that in the case of *Crocker* v. *Malley* this Court had before it the provisions of an act levying an income tax and in which Congress imposed the tax on individuals as well as corporations. In other words, for the purpose of the imposition of the income tax, Congress has consistently classified taxpayers as individuals and as corporations, and a pure trust is taxable as an individual and an association as a corporation. The question here involved is simply that of the proper classification of the taxable entity, as an individual or as a corporation. There is present no question of escaping tax liability as in *Hecht* v. *Malley*, below. Under the question is that of double tax liability as in *Crocker* v. *Malley*.

Before passing on from the case of *Crocker* v. *Malley*, the Court's attention is invited to the similarity of the facts in that

case and in the instant case. In both cases, there was an ordinary real estate trust, the beneficiaries had no voice in the management and in neither case did the trust bear any resemblance to a corporation.

In the case of *Hecht* v. *Malley*, 265 U. S. 144, decided by this Court May 12, 1924, the tax involved was not the income tax but the capital stock tax, an excise tax levied on corporations but not on individuals. The case did not involve the classification of a taxpayer as an individual or as a corporation. Among the cases there before this Court was the Crocker trust which was the petitioner in *Crocker* v. *Malley, supra,* but the terms of the trust instrument had been amended and the trustees had greatly increased their activities. The specific provision of law there before this Court was Section 407 of the Revenue Act of September 8, 1916, (39 Stat. 756) and Section 1000 of the Revenue Act of 1918, Act of February 24, 1919, (40 Stat. 1057) in which the capital stock tax was imposed on "every corporation, joint-stock company or association." The tax imposed was, however, the special excise tax, the imposition of which has been held to be constitutional only when imposed on the privilege of doing business. *Ray Consolidated Copper Company*, 268 U. S. 273. In the case of *Hecht* v. *Malley, supra,* which involved the capital stock tax, this Court had before it as one of the bases for the imposition of tax the question of the carrying on or doing business which was not before this Court in the previous case of *Crocker* v. *Malley, supra.*

In the opinion of Mr. Justice Sanford in the case of *Hecht* v. *Malley,* that and the *Crocker* v. *Malley* cases are distinguished with the following explanations:

> The trustees of the Hecht and Hay-Market Trust earnestly rely, however, upon the decision in *Crocker* v. *Malley*, 249 U. S. 223, 63 L. ed. 573, 2 A. L. R. 1601, 39 Sup.

Ct. Rep. 270, as conclusively determining that they cannot be held to be "associations" unless the trust agreements vest the shareholders with such control over the trustees as to constitute them more than strict trusts within the Massachusetts rule. This case arose under No. II. G(a), of the Income Tax Act of October 3, 1913, imposing a tax upon the net income of 'every corporation, joint-stock company or association * * * organized in the United States, no matter how created or organized." (38 Stat. at L. 172, chap. 16, 4 Fed. Stat. Anno. 2d ed. p. 245.) Section II.D provided that trustees or other fiduciaries were exempt from this tax upon dividends received from corporations taxable upon their net income. The precise question was whether the trustees of the Wachusett Realty Trust were subject to the income tax upon dividends received from a Massachusetts corporation that was itself taxable upon its net income. The trustees insisted that they were not an "association" subject to this tax, under G(a), but merely trustees, and entitled to the exemption as fiduciaries under D. The trust had been created by a Maine corporation which contemplated dissolution, for the benefit of its shareholders. It had transferred to the trustees the fee of certain lands leased to a Massachusetts manufacturing corporation engaged in operating several mills, and also the stock in that corporation which it held. The purpose of the trust was to convert this property into money and distribute the net proceeds to the beneficiaries, within a period left to the discretion of the trustees. Meanwhile they were to distribute the net income, but could apply any funds for the repair and development of the property or the acquisition of other property, pending conversion and distribution. Their function, as emphasized in the opinion, was not to manage the mills, but simply to collect the rents and income, with a large discretion in its application. The beneficiaries had no control except in certain matters in which their consent was required.

The Court, after stating that the declaration of trust on its face was "an ordinary real estate trust of the kind

familiar in Massachusetts," and that there "could be little doubt that in Massachusetts this arrangement would be held to create a trust and nothing more," said that "as the plaintiffs undeniably are trustees; if they are to be subjected to a double liability the language of the statute must make the intention clear;" and that "it would be a wide departure from a normal usage to call the beneficiaries here a joint-stock association when they are admitted not to be partners in any sense, and when they have no joint action or interest and no control over the fund. On the other hand, the trustees by themselves cannot be a joint-stock association within the meaning of the act unless all the trustees with discretionary powers are such, and the special provision for trustees in D is to be made meaningless. We perceive no ground for grouping the two—beneficiaries and trustees—together, in order to turn them into an association, by uniting their contrasted functions and powers, although they are in no proper sense associated. * * * We presume that the taxation of corporations and joint-stock companies upon dividends of corporations that themselves pay the income tax was for the purpose of discouraging combinations of the kind now in disfavor, by which a corporation holds controlling interests in other corporations which, in their turn, may control others, and so on, and in this way concentrates a power that is disapproved. There is nothing of that sort here. Upon the whole case we are of opinion that the statute fails to show a clear intent to subject the dividends on the Massachusetts corporation's stock to the extra tax imposed by G(a)."

This opinion is based primarily upon the view that the Income Tax Act, considering its purpose, did not show a clear intention to impose upon the trustees, as an "association," a double liability in reference to the dividends on stock in the corporation that itself paid an income tax, when, considered as "trustees," they were, by another provision of the act, exempt from such payment. And the language used arguendo in reaching this conclusion that the trustees could not be deemed an association unless all trustees with discretionary powers are such, and that

there was no ground for grouping together the beneficiaries and trustees in order to turn them into an association, is to be read in the light of the trust agreement there involved, under which the trustees were, in substance, merely holding property for the collection of the income and its distribution among the beneficiaries, and were not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business. *Zonne* v. *Minneapolis Syndicate*, 220 U. S. 187, 190, 55 L. ed. 428, 430, 31 Sup. ct. Rep. 361. And see *Smith* v. *Anderson*, L. R. 15 Ch. Div. 247, 50 L. J. Ch. N. S. 39, 43 L. T. N. S. 329, 29 Week Rep. 21.

It results that *Crocker* v. *Malley is not an authority for* the broad proposition that, under an act imposing an excise tax upon the privilege of carrying on a business, a Massachusetts trust engaged in the carrying on of business in a quasi corporate form, in which the trustees have similar or greater powers than the directors in a corporation, is not an "association" within the meaning of its provisions.

We conclude, therefore, that when the nature of the three trusts here involved is considered, as the petitioners are not merely trustees for collecting funds and paying them over, but are associated together in much the same manner as the directors in a corporation for the purpose of carrying on business enterprises, the trusts are to be deemed associations within the meaning of the Act of 1918; this being true independently of the large measure of control exercised by the beneficiaries in the Hecht and Haymarket Cases, which much exceeds that exercised by the beneficiaries under the Wachusett Trust. We do not believe that it was intended that organizations of this character—described as "associations" by the Massachusetts Statutes, and subject to duties and liabilities as such—should be exempt from the excise tax on the privilege of carrying on their business merely because such a slight measure of control may be vested in the beneficiaries that they might be deemed strict trusts within the rule established by the Massachusetts Courts.

The petitioners submit that the instant case is readily distinguishable from *Hecht* v. *Malley, supra,* on the following grounds:

1. The trustees were not actually engaged in carrying on a business in a quasi corporate form. On the contrary they were merely conserving the corpus of the trust and collecting and distributing income.

2. The trustees were not associated together with similar or greater powers than the directors of a corporation. The powers of the trustees were those usual in a pure trust.

3. The certificate holders had no voice in the management and no meetings were provided for. This distinguishes the instant case from *Hecht* v. *Malley* and places it in the same class as *Crocker* v. *Malley*.

4. The provisions of the Act before this Court in *Hecht* v. *Malley* had not been made the subject of regulations by the Treasury Department. In the instant case the regulations under previous acts are to be considered as law.

5. There is the further distinction that in the case of *Hecht* v. *Malley* the tax involved was an excise tax on carrying on or doing business, while in the instant case the tax is the income tax and the question is not that of tax exemption in any sense but merely that of the classification of the taxpayer as an individual or a corporation.

The most recent decision of this Court having any bearing on the question here involved appears to be *Senior* v. *Braden*, decided May 20, 1935, 79 L. ed. 863, which involved a taxing act of the State of Ohio. In his opinion Mr. Justice McReynolds refers to *Hecht* v. *Malley, supra,* as authority that a test for classifying a trust as an association is the voice of the beneficiaries in the management. The following is quoted from the opinion in that case:

Each trustee holds only one piece of land and is free from control by the beneficiaries. They are not joined with it in management.

The petitioners submit that the facts in the instant and those in *Crocker* v. *Malley, supra,* are similar and that the question is the same and that the decision of this Court in that case is controlling.

POINT B.

The Word "Associations" in the Several Revenue Acts is Grouped With the Terms "Joint-Stock Companies" and "Insurance Companies" and is to be Construed to Include Only Such Associations as are Properly Comparable to Corporations, Joint-Stock Companies or Insurance Companies. The Applicable Rule of Statutory Construction is that the Term is to be Construed with Reference to the Context of the Statutory Provision in which it Appears.

This Court in *Hecht* v. *Malley, supra,* stated that the word "association" appears to be used, in the act there under consideration, in its ordinary meaning and the Court referred to definitions previously given the term. In the course of his opinion, Mr. Justice Sanford stated:

> It has been defined as a term "used throughout the United States to signify a body of persons united without a charter, but upon the methods and forms used by incorporated bodies for the prosecution of some common enterprise." 1 Abbott's Law Dict. 101 (1879); I Bouvier's Law Dict. Rawle's 3d Rev. p. 269; 3 Am. & Eng. Enc. Law, 2d ed. 162; and *Allen* v. *Stevens,* 33 App. Div. 485, 54 N. Y. Supp. 8, 23, in which this definition was cited with approval as being in accord with the common understanding. Other definitions are: "In the United States, as distinguished from a corporation, a body of persons organized for the prosecution of some purpose, without a charter, but having the general form and mode of procedure of a corporation." Webster's New Int. Dict. "(U. S.) An organized but unchartered body analogous

> to, but distinguished from, a corporation." Pract. Stand. Dict. * * *
>
> We think that the word "association," as used in the act, clearly includes "Massachusetts trusts" such as those herein involved, having quasi corporate organizations under which they are engaged in carrying on business enterprises. What other form of "associations," if any, it includes, we need not, and do not, determine.

It is to be noted that in both the definitions quoted and in this Court's own definition that an association is a quasi corporation or has the general form and mode of procedure of a corporation.

The word "associations" appears in Section 2 of both the Revenue Acts of 1924 and 1926. In both acts this section is in part:

> When used in this Act—
>
> (1) The term "person" means an individual, a trust or estate, a partnership, or a corporation.
>
> (2) The term "corporation" includes associations, joint-stock companies, and insurance companies.

Embraced in the definition of the term "person" and as separate and distinct taxpayers are trusts and corporations. Trusts are taxable as individuals under Section 219 of each Act and corporations are subject to a different tax under Section 230 of each Act.

In addition to being included in the definition of "corporation" the term "associations" is grouped with the terms "joint-stock companies" and "insurance companies". By the use of the term "associations" Congress meant something comparable to a joint-stock company or an insurance company, certainly something in the nature of a company. There is today but little difference between a joint-stock company and a corporation and it is not improper to call such company a quasi corporation, 33 C. J. 879. In using the term "insurance com-

panies" Congress clearly meant corporation engaged in the business of insuring.

The rule of construction that should be followed here is therefore that the word "associations" should be held to mean such taxpayers as are comparable to "joint-stock companies" and "insurance companies".

We are here concerned with "property held in trust" within the express provisions of Section 219 of both the 1924 and 1926 Acts entitled "Estates and Trusts". Equally with the provisions of Section 2 in which associations are classed as corporations the petitioners submit force should be given to Section 219 under the general language of which the trust here involved necessarily falls because property is held in trust and this Court must find that the trust comes clearly within the intendment of Section 2 before the petitioners can be excluded from the terms of Section 219 and taxed as an association or corporation under Section 230. As stated in *Coleman-Gilbert Associates* v. *Commissioner*, 76 Fed. (2d) 191, 195:

> The imposition of a double tax upon the income of the trust as an entity, and a further tax upon the distributive shares of the beneficiaries, should clearly be warranted under the acts of Congress, and should not have as its basis some remote resemblance to a corporation. If there is doubt, it should be resolved in favor of the taxpayer. Citing *Crocker* v. *Malley* and *Hecht* v. *Malley*.

POINT C.

The True Test to be Applied is Whether the Trustees Act or Carry on Business After the Form and Manner of a Corporation. This Requires a Quasi-Corporate Corporation in Which the Beneficiaries Have Some Voice in the Management.

As pointed out in *Coleman-Gilbert Associates* v. *Commissioner*, 76 Fed. (2) 191, First Circuit, Congress has not under-

taken to lay down any tests for determining whether an organization is an association or a pure trust.

> "As yet the Supreme Court has not laid down any absolute tests. * * * The Treasury Department has endeavored from time to time to clarify the situation by regulations defining associations and trusts. * * *
>
> "We think, however, it is generally agreed that, in order for a trust to be taxed as a corporation, the trustees must not only be carrying on a business enterprise for profit, but must be doing it in much the same manner and form as directors of a corporation. One other factor also seems to be agreed upon: that it is not what the trustees are authorized to do under the trust instrument, but what they actually are doing. *Gardiner* v. *United States*, 49 Fed. (2d) 992; *Commissioner* v. *Pryor & Lockhart Development Co.*, (70 Fed. (2d) 154)."

In *Hecht* v. *Malley, supra*, this Court gives as its definition of an association a quasi-corporate organization.

The Board of Tax Appeals, following the rule laid down in *Sturgeon* v. *Commissioner*, 25 B. T. A. 368, has consistently stated as a requirement for an association that the beneficiaries shall have associated themselves in the general form and manner of procedure of a corporation.

The petitioners are trustees "of property held in trust" within the exact wording of Section 219 and are not to be compared with the directors of a quasi-corporation, and they are not engaged in doing business in the form or mode of procedure of a corporation. Under the test laid down by the Board itself; the trustees should not be taxed as a corporation but as a pure trust.

The Board held that for the year 1923 the petitioners are taxable as a trust, and the petitioners submit that the provisions of several revenue acts are identical and that the same

tests should be applied to the years 1924, 1925 and 1926 that were applied to the year 1923, and the decision should be that the declaration did not create a quasi-corporate organization, that the trustees did not act in the form and mode of procedure of a corporation and that the beneficiaries had no voice in the conduct of the business.

The instant case differs necessarily from cases in which persons are associated together for the purpose of manufacturing or merchandising in which the primary object is to do business rather than to hold property. In the case, *Reinecke* v. *Kaenpfer*, 72 Fed. (2d) 469, the trustees were associated to carry on the business of selling bird seed. The purpose of the association was necessarily the merchandising of bird seed. The trustees were held taxable as an association following *Hecht* v. *Malley, supra,* on the ground that the petitioners were not merely trustees for collecting funds and paying them over, but were associated in much the same manner as directors in a corporation for the purpose of carrying on a business enterprise. In the instant case, the purpose of the trust is not to engage in a manufacturing or merchandising business or to associate the various interested persons as a company for the conduct of business, but is merely to place the title to a certain tract of real estate in trustees to be disposed of by them and the venture concluded.

The test which in certain cases has been followed by the Board of Tax Appeals is that stated in *Sturgeon* v. *Commissioner*, 25 B. T. A., 368, 374:

> This Board has held that the significant tests to be applied in determining whether an alleged trust is a trust, or an association taxable as a corporation, are whether (1) the beneficiaries of the alleged trust have voluntarily associated themselves together in the general form and mode of procedure of a corporation, and (2) are organized to, and in fact, are engaged in the active conduct of

> a business for profit, or (3) whether the trustees are merely holding the property and collecting the income therefrom and distributing to those beneficially interested. *Extension Oil Co.*, 16 B. T. A. 1028; affd., 47 Fed. (2d) 65; *Jackson-Wermich Trust*, 24 B. T. A. 150; *E. B. Galbreath et al.*, 24 B. T. A. 1107.

In the instant case the Board did, however, apparently not so much heed its own tests as it did the decision of the Circuit Court of Appeals for the Ninth Circuit, by which its decision was reviewable, in the case of *Sloan* v. *Commissioner*, 63 Fed. (2d) 666. In that case, as in this, the petitioners submit, the Court went far beyond the terms of the revenue act and the provisions of the regulations in holding that trustees, engaged merely in collecting and distributing installment payments, were doing business in the form and manner of a corporation. As stated in *Commissioner* v. *Kelley*, 74 Fed. (2d) 71, 74:

> there is no law prohibiting trustees from carrying on business for profit; but if the trustees are given absolute control over the business and the cestuis qui trustent have no control, either over the trustees or the business, such a trust is not taxable as a corporation.

In *Bouchard* v. *First People's Trust*, 253 Mass. 351, it was held that the trust was not an "association" within the meaning of G. L. c. 182, Sec. 6, permitting a suit against an association for acts of trustees and the Court said at pages 360-361:

> "It seems plain to us that there is no association, in the sense in which that word is commonly used, among the shareholders of the First People's Trust. Each of them has simply a property interest in a fund held for their common benefit. The arrangement established by the declaration of trust involves a total want of legal power by the shareholders as to the trust. They have no voice direct or remote in its management. They cannot exercise the slightest control over the selection or conduct of the trus-

tees. No question as to its execution can be ever submitted to them for approval or even for advice. Each shareholder by subscribing for a certificate, which is by individual choice and not by joint action, surrenders to those, who are and from time to time become trustees by the self-perpetuating selection of the trustees for the time being, all legal power over the money paid for the subscription. The shareholders are unassociated; they have no organization; each of them has simply an equitable interest in the trust. The various definitions of the word 'association' all imply, if they do not require, as an essential element, that there be some form of organization resembling modes of procedure inherent in incorporated bodies. A business corporation is unthinkable where the shareholders are devoid of legal rights, have no officers and are and must remain forever dumb as to the selection, approval or disapproval of managers and methods of conduct of corporate affairs."

POINT D.

The Mere Fact that the Trustees Retained Title to Land and Shares of Corporate Stock and Collected and Distributed Income Does Not Amount to Doing Business as Contemplated by This Court in Hecht v. Malley.

The Court below, following its previous decisions, applied what it termed the business test and held that the meager activities of the trustees constituted doing business and hence the trustees are to be taxed as an association. In the opinion it is stated:

> As to the contention that "doing business" is not controlling or relevant, this court in *Twin Bell Oil Syndicate* v. *Helvering*, 70 F. (2d) 402 (C. C. A. 9), after quoting from its opinion in the *Trust No. 5833, Security First National Bank* v. *Welch*, 54 F. (2d) 323 (C. C. A. 9), said at page 407:
>
> > "There is ample additional authority for the proposition that the 'business' test is now paramount."

This Court has not held that business activity alone is sufficient to require that a trust be classified as an association. In *Hecht* v. *Malley, supra,* this Court clearly pointed out that the organizations there under consideration were not merely doing business but the doing of business was after the form and methods of a corporation. The petitioners submit that there is a wide distinction between mere business activity and the conduct of business after the form and manner of a corporation. Business is conducted by individuals and partnerships as well as by corporations. The mere act of doing business or the mere fact that some business is done is not the sole test. The business activity is looked to merely for the purpose of determining the manner in which done. The test is, therefore, the manner of doing business and not the fact of doing business.

In the present case, the trustees were merely holding title to property and as necessary incidents thereto were receiving the purchase price for property previously sold and income and dividends and were distributing money so received to beneficiaries. These activities are such as are necessarily incident to the ownership of property and bear no resemblance to the conduct of business in the form and manner of a corporation.

What constitutes carrying on or doing business is, of course, difficult to define, but the question has been considered by a number of the lower courts in connection with the capital stock tax, which to be constitutional requires that the taxpayer be carrying on or doing business. The courts have consistently held that a taxpayer, whether or not a corporation, whose activities are confined to the preservation of property and the collection and distribution of income, are not carrying on or doing business and not subject to the capital stock tax. See *Fink Coal and Coke Company* v. *Heiner,* 26 Fed. (2d) 136; *Lane Timber Company* v. *Hynson,* 4 Fed. (2d) 666; *Cannon*

v. *Elk Creek Lumber Company*, 8 Fed. (2d) 996 and *Clallon Lumber Company* v. *United States* (D. C.) 34 Fed. (2d) 994.

POINT E.

The Activities Actually Engaged in by the Trustees, Rather Than the Possible Activities Authorized by the Declaration of Trust, are to be Considered in Determining Whether or not they were Acting or Carrying on Business in the Form and Manner of a Corporation.

There is apparent unanimity of decision that in determining the classification of a trust as a pure trust or as an association the actual activities of the trustees are to be looked to rather than those authorized by the trust instrument but not exercised by the trustees. See *Commissioner* v. *Brouillard*, 70 Fed. (2d) 54, Tenth Circuit; *Tyson* v. *Commissioner*, 54 Fed. (2d) 29, Seventh Circuit; *Commissioner* v. *Duckwitz*, 68 Fed. (2d) 629, Seventh Circuit; *Dunbar* v. *Commissioner*, 65 Fed. (2d) 447, First Circuit and *Gardiner* v. *U. S.*, 49 Fed. (2d) 992, First Circuit. In the last mentioned case it is stated, "The crucial test must be found in what the trustees actually do, not in the mere existence of long unused broad powers."

The record clearly sets forth the activities actually engaged in by the trustees which, except for the insignificant period of twelve days, consisted simply in the retention of title to property, the principal part of which had previously been disposed of under sales contracts, the collection of the sales price and the formal conveyance of title, the collection of income and the distribution of both the purchase price and the income to the beneficiaries of the trust. These activities appear in the record as follows:

> (1) operation of said golf course for the first 12 days of 1924 as aforesaid, (2) Receipt from collection agent bank of principal and interest so collected by said bank in behalf

of petitioner, (3) Receipt of credit of interest earned on bank balances, (4) Receipt of assignment fees in assignment of lot purchase contracts by holders thereof, (6) Receipt of dividends from Western Avenue Golf Club, Inc., upon shares thereof owned by petitioner, (7) Distribution of moneys to holders of beneficial interests in petitioner trust by way of dividends and, in some cases, by way of redemption and retirement of their beneficial interests.

It is to be remembered that all real estate had been sold or agreed to be sold, that the stock holdings were acquired in exchange for a part of the land and that all that the trustees were in fact doing was collecting the income and distributing it. Under the provisions of Article 1504, as variously amended, of Regulations 45, 62, 65 and 69, the trust should be classed as a holding trust or as one merely holding property for the collection and distribution of income with ultimate liquidation in view on the termination of a single venture.

POINT F.

The Provisions of the Revenue Act of 1924 are to be Construed as Incorporating Previous Treasury Department Regulations in Force at the Time the Provisions of Existing Laws were Re-enacted, and for that Year there is no Doubt but that the Trustees are to be Taxed as a Pure Trust. At the Time of the Enactment of the Revenue Act of 1926, the Regulations had not been Materially Changed, and Thereunder the Trustees Should be Taxed as a Pure Trust.

The years here involved are 1924, the tax for which is imposed by the Revenue Act of 1924, and 1925 and 1926, the tax for which is imposed by the Revenue Act of 1926. The provisions relating to associations and trusts in these acts as well as in the Revenue Act of 1918 (40 Stat. 1057) and in the Revenue Act of 1921 (42 Stat. 222) are identical. The pro-

visions of these earlier acts have, therefore, been reenacted without change, and such regulations as were promulgated for the enforcement of the Revenue Act of 1918 and the Revenue Act of 1921 and which were in force at the time of the enactment of the Revenue Act of 1924 and the Revenue Act of 1926 have, therefore, the force and effect of law.

In each of the revenue acts, provision is made for the promulgation of regulations by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury. This provision is, of course, to be construed to mean that the Commissioner has authority to promulgate merely such rules and regulations as are administratively necessary. The Commissioner, of course, does not have authority in any way to alter the provisions of the current act. Further, his interpretation of the current act is not in any sense binding on the courts.

But when the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury has promulgated regulations for the enforcement of the revenue act, or acts, and has consistently applied his regulations, and then Congress reenacts the same statutory provisions, the rule of statutory construction, binding on the courts, is that Congress by reenacting the statute without change adopts the administrative construction in the regulations and those regulations become law.

In Regulations 45, promulgated under the Revenue Act of 1918, the Treasury Department in Articles 1502 and 1504 undertook to define an association or to prescribe tests for the determination of what constitutes an association and also to distinguish an association from a pure trust. Article 1502 provides that associations include trusts and organizations which act or do business in an organized capacity and the income of which is distributed or distributable among members.

This article of the regulations applies as the test the acting or doing business in an organized capacity: This test is so general as to be of but little help. This article of the regulations has been promulgated without material change in all subsequent regulations. The change made in Article 1502 of Regulations 62 is that a corporation which has ceased to exist in law but continues its business in corporate form; it is taxable as an association, but if it continues its business as a trust, it is subject to the provisions of section 219. This was repeated in Regulations 65. This added provision in Regulation 62 sets forth the clearest possible distinction between an association and a trust. The exact words of the Regulations are:

> A corporation which has ceased to exist in contemplation of law but continues its business in corporate form is an association or corporation within the meaning of Section 2, but if it continues its business in the form of a trust, it becomes subject to the provisions of Section 219.

In reenacting Section 2 of the Revenue Act of 1921 without change, Congress incorporated and read into the Revenue Act of 1924 this distinction between an association and a pure trust, that an association "continues its business in corporate form" and a pure trust "continues its business in the form of a trust."

Article 1504 of Regulations 45 provides that if the cestuis que trusts have a voice in the conduct of the business, a commonlaw trust is an association.

Regulations 62, promulgated for the Revenue Act of 1921, reprinted without change the above provision of Regulations 45.

The regulations in force at the time of the enactment of the Revenue Act of 1924 were, therefore, Regulations 45 and Regulations 62, and when Congress reenacted in the Revenue Act of 1924 the provision of the Revenue Act of 1918 and the Revenue Act of 1921, that the term "corporation" includes

an association, it approved and adopted the construction placed on that provision in the prior regulations. Article 1504 of both regulations is:

> Where trustees hold real estate subject to a lease and collect the rents, doing no business other than distributing the income less taxes and similar expenses to the holders of their receipt certificates, who have no control except the right of filling a vacancy among the trustees and of consenting to a modification of the terms of the trust, no association exists and the cestuis que trust are liable to tax as beneficiaries of a trust, the income of which is to be distributed periodically, whether or not at regular intervals. But in such a trust if the trustees pursuant to the terms thereof have the right to hold the income for future distribution, the net income is taxed to the trustees instead of to the beneficiaries. See Section 219 of the statute and Articles 341-347. If, however, the cestuis que trust have a voice in the conduct of the business of the trust, whether through the right periodically to elect trustees or otherwise, the trust is an association within the meaning of the statute.

It is, therefore, submitted that insofar as the Revenue Act of 1924 is concerned, its provisions must be given the same construction that the regulations and the Commissioner's rulings had been given to the prior acts.

When the Commissioner came to promulgate rulings for the enforcement of the Revenue Act of 1924, he made a change in Article 1504 and attempted to distinguish between holding trusts and operating trusts. It is submitted, however, that the regulations made after the enactment of the Revenue Act of 1924 cannot be looked to find the intent of Congress in the interpretation of the act and are in no sense binding on the courts. The point the petitioners desire to make is that a regulation pertaining to a prior law, reenacted without change,

has the approval of Congress and has the effect of law, but that a regulation subsequently promulgated does not.

When we come to the year 1925 and 1926 and to the construction of the Revenue Act of 1926, consideration must, of course, be given to the changes in the regulations, if any. In Regulations 65, for the enforcement of the Revenue Act of 1924, promulgated October 6, 1924, Article 1502 was printed without material change, but Article 1504 was changed to distinguish between holding trusts and operating trusts. By Treasury Decision 3748 and on August 31, 1925, the regulation was amended to define as a pure trust the holding of property by the trustees without control by the beneficiaries and to define as an association a trust in which the beneficiaries have positive control, and further the regulations stated that even in the absence of control by the beneficiaries where the trustees are not restricted to the collection and distribution of income but are associated together with similar powers to the directors of a corporation for the purpose of carrying on a business enterprise, the trust should be classed as an association. Article 1504 of Regulations 65 as so amended reads:

> Where trustees merely hold property for the collection of the income and its distribution among the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, and the beneficiaries have no control over the trust although their consent may be required for the filling of a vacancy among the trustees or for a modification of the terms of the trust, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by Section 219 and by Articles 341-347. If, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists within the meaning of Section 2. Even in the absence of any control by the beneficiaries, where the trustees are not restricted to the

> mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the statute.

This was the state of the regulations at the time of the enactment of the Revenue Act of 1926, and it is submitted that these changes were known to Congress and should, of course, be resorted to in the construction of the Revenue Act of 1926, if these changes are in fact material. It is, therefore, in order to read Treasury Decision 3748 in conjunction with Section 2(a) of the Revenue Act of 1926 (44 Stat. 9).

The trustees in the instant case were merely holding property "for the collection of the income and its distribution among the beneficiaries of the trust" and were not engaged "in the carrying on of any business" and the beneficiaries had no control over the trust within the exact wording of Article 1504 of Regulations 65, as amended by Treasury Decision 3748, in force at the time of the enactment of the Revenue Act of 1926. As a matter of fact the trustees are taxable as a pure trust within the express terms of Article 1504 of Regulations 69 promulgated for the enforcement of the Revenue Act of 1926 and which article is the same as Treasury Decision 3748.

POINT G.

Pursuant to the Retroactive Provisions of Section 704 of the Revenue Act of 1928, the Trustees are Taxable as a Trust Because they Filed a Return as a Trust and were Considered to be Taxable as a Trust Under Regulations in Force at the Time the Return was Made. The Section by its Express Terms Embraces all Years Prior to 1925.

In Section 704 of the Revenue Act of 1928, (45 Stat. 880) which is retroactive, provision is made that for years prior to

1925 a taxpayer shall be taxable as a pure trust and not as a corporation if the taxpayer was considered to be taxable as a trust and not as a corporation under the regulations in force at the time the return was made. Section 704 is, therefore, to be read as a part of the Revenue Act of 1924. Section 704 in part is:

> (a) If a taxpayer filed a return as a trust for any taxable year prior to the taxable year 1925 such taxpayer shall be taxable as a trust for such year and not as a corporation, if such taxpayer was considered to be taxable as a trust and not as a corporation either (1) under the regulations in force at the time the return was made or at the time of the termination of its existence, or (2) under any ruling of the Commissioner or any duly authorized officer of the Bureau of Internal Revenue applicable to any of such years, and interpretative of any provision of the Revenue Act of 1918, 1921 or 1924, which had not been reversed or revoked prior to the time the return was made, or under any such ruling made after the return was filed which had not been reversed or revoked prior to the time of the termination of the taxpayer's existence.

The position of the petitioners is that under the regulations in force at the time the return for 1924 was filed, the petitioners should be classed as a pure trust and not as a corporation, this for the two reasons (1) that the regulations in force at the time of its passage are part of the act and (2) that Section 704 of the Revenue Act of 1928 so provides.

The Board of Tax Appeals held that pursuant to the provisions of Section 704 of the Revenue Act of 1928 and of the appropriate regulations in existence at the time the return was filed that the petitioners are taxable as a pure trust for 1923, but for the year 1924 the Board held that the petitioners are taxable as a corporation. The reasoning of the Board appears to be that a change in regulations dated from May 12,

1924, when this Court handed down the decision in *Hecht* v. *Malley, suprd.* The Board used as the basic date the date of the decision of this Court rather than August 31, 1925, when Regulations 65, Article 1504 were amended to give effect to what the Treasury Department considered to be the proper application of the decision of this court in an income tax case. In its opinion, the Board stated:

> We have heretofore held in applying this section of the Act that under the Commissioner's Regulations and Bureau Rulings, in effect up to and including the calendar year 1923, and prior to the change in the Commissioner's Rulings giving effect to the decision in *Hecht* v. *Malley*, 265 U. S. 144, decided May 12, 1924, the test to be applied in distinguishing trusts from associations was whether the beneficiaries or shareholders controlled the action of the trustees.

The reasoning of the Board is that the regulations were changed immediately on the rendition of the decision of this Court in the case of *Hecht* v. *Malley* on May 12, 1924, while as a matter of fact, the actual amendment to the regulations was not promulgated until August 31, 1925, and after the petitioners had filed the return for the year 1924.

It is, therefore, the position of the petitioners that the Board of Tax Appeals has placed an erroneous construction on Section 704 of the Revenue Act of 1928. We are here concerned with the construction of the provision of the Act of 1928 as well as of the provisions of the Act of 1924. The specific provision of Section 704 is that a taxpayer shall be taxable as a trust if under "the regulations in force at the time the return was made" the taxpayer was taxable as a pure trust and not as a corporation.

In Section 704, no reference is made to the decisions of the courts.

The regulations which were in force at the time the return was filed are, therefore, those contained in Article 1504 of Regulations 65 in which trusts are classified as holding trusts and operating trusts and in which holding trusts are referred to as those in which the trustees merely hold property for the collection and disbursement of income and in which operating trusts are referred to as those in which the trustees are not merely engaged in the collection and distribution of income but are associated together in much the same manner as directors in a corporation for the purpose of carrying on some business enterprise.

Under this provision of the regulations it is respectfully submitted that the petitioners should be taxed as a pure trust for the year 1924, for Congress has very clearly indicated in the reference to years prior to 1925 that a trust, such as the one here under consideration, should under all regulations prior to August 31, 1925, be taxed as a pure trust and not as an association.

VIII.

CONCLUSION.

The petitioners submit that they are, within the meaning of Section 219 of the Revenue Acts of 1924 and 1926, trustees "of property held in trust" consisting of that part of the land originally placed in trust which finally had not been disposed of and of the shares of corporate stock received in exchange for another part of the real estate and that they should be taxed as a trust and not as an association for the reason that the petitioners were simply holding title to the land and the shares of corporate stock and collecting and distributing the avails thereof to the beneficiaries of the trust. They were not carrying on or doing business after the form or manner of a corporation and they were not acting in the manner of a board

of directors and the beneficiaries had no voice in the management of the trust as do stockholders in a corporation.

The petitioners further submit that for the year 1924 they should be taxed as a trust under both the regulations in force at the time of the enactment of the Revenue Act of 1924 and under the express provisions of Section 704 of the Revenue Act of 1928.

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FILE COPY

No. [redacted] 17.

In the Supreme Court of the United States

OCTOBER TERM, 1934

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES OF AN EXPRESS TRUST, KNOWN AS WESTERN AVENUE GOLF CLUB, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

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In the Supreme Court of the United States

OCTOBER TERM, 1934

No. 834

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES of an Express Trust, Known as Western Avenue Golf Club, petitioners

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion of the United States Board of Tax Appeals (R. 31–51) is not reported. The opinion of the Circuit Court of Appeals (R. 67–72) is reported in 74 F. (2d) 803.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 7, 1935 (R. 73). A petition

for rehearing was denied March 1, 1935. The petition for writ of certiorari was filed April 1, 1935. The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1935.

QUESTION PRESENTED

Whether the trust in question is an association.

STATUTES AND REGULATIONS INVOLVED

The statutes and regulations involved are set out in the Appendix, *infra*, pp. 5–7.

STATEMENT

The facts as stipulated (R. 22–31) and as found by the Board (R. 33–45) may be summarized as follows:

On October 4, 1921, T. A. Morrissey and James M. O'Brien executed a declaration of trust to certain real estate in Los Angeles, California, a part of which was converted into a golf course operated for a time by the trust (hereinafter referred to as the petitioner), and the remainder subdivided into lots for sale. Prior to the taxable years 1924, 1925, and 1926, the club was transferred to a corporation for all of its capital stock. Thereafter, and until January 12, 1924, the petitioner operated it under a lease, when its operation by the petitioner ceased. There were 2,000 shares of common and a like amount of preferred stock. Man-

agement of the trust was vested in trustees, the shareholders having no rights, except to dividends. During the taxable years the activities of the trust were reduced to (1) the operation of the golf course as indicated above, (2) the conveyance of lots to purchasers, and (3) the collection of moneys due the trust and their distribution to the holders of beneficial interests therein by way of dividends, and, in some cases, by way of redemption and retirement of such interests.

The petitioner filed a trust return for each of the years of its existence. The Commissioner determined that it was an association, with resultant deficiencies in each of the taxable years. The Board sustained such determination, and the Circuit Court of Appeals affirmed the Board.

ARGUMENT

We recognize that, as stated by the petitioner in this case, there is much confusion in the Circuits in the interpretation and application of the rule laid down by this Court in *Hecht* v. *Malley*, 265 U. S. 144.

However, we think the court below correctly applied the rule in this case, and since in other cases presenting this issue this Court has refused to grant certiorari, we feel we should oppose the granting of the writ in this case. See *United States* v. *Neal*, 28 F. (2d) 1022 (C. C. A. 1st), certiorari denied, 278 U. S. 659; *Little Four Oil & Gas Co.* v. *Lewellyn*, 35 F. (2d) 149 (C. C. A.

3d), certiorari denied, 280 U. S. 613; *Allen v. Commissioner,* 49 F. (2d) 716 (C. C. A. 2d), certiorari denied, 284 U. S. 655; *Trust No. 5833, Security-First Nat. Bank v. Welch,* 54 F. (2d) 323 (C. C. A. 9th), certiorari denied, 286 U. S. 544; *Gray v. Hopkins,* 68 F. (2d) 561 (C. C. A. 5th), certiorari denied, 292 U. S. 643; *Tyson* v. *Commissioner,* 68 F. (2d) 584 (C. C. A. 7th), certiorari denied, 292 U. S. 657; and *Commissioner* v. *Pryor & Lockhart Development Co.,* 70 F. (2d) 154 (C. C. A. 10th), certiorari denied, 293 U. S. 574.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition should be denied.

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MAY 1935.

APPENDIX

Revenue Act of 1924, c. 234, 43 Stat. 253:

SEC. 2. (a) When used in this Act—

* * * * *

(2) The term "corporation" includes associations, joint-stock companies, and insurance companies. (U. S. C., Title 26, Sec. 1262.)

Section 2 (a) (2) of the Revenue Act of 1926, c. 27, 44 Stat. 9 (U. S. C. App., Title 26, Sec. 1262), is identical with the provisions of Section 2 (a) (2) of the Revenue Act of 1924, *supra*.

Revenue Act of 1928, c. 852, 45 Stat. 791, 880:

SEC. 704. TAXABILITY OF TRUSTS AS CORPORATIONS—RETROACTIVE.

(a) If a taxpayer filed a return as a trust for any taxable year prior to the taxable year 1925 such taxpayer shall be taxable as a trust for such year and not as a corporation, if such taxpayer was considered to be taxable as a trust and not as a corporation either (1) under the regulations in force at the time the return was made or at the time of the termination of its existence, or (2) under any ruling of the Commissioner or any duly authorized officer of the Bureau of Internal Revenue applicable to any of such years, and interpretative of any provision of the Revenue Act of 1918, 1921, or 1924, which had not been reversed or revoked prior to the time the return was made, or under any such ruling made after the return was filed which had not been reversed or

revoked prior to the time of the termination of the taxpayer's existence.

(b) For the purpose of the Revenue Act of 1926 and prior Revenue Acts, a trust shall, at the option of the trustee exercised within one year after the enactment of this Act, be considered as a trust the income of which is taxable (whether distributed or not) to the beneficiaries, and not as an association, if such trust (1) had a single trustee, and (2) was created and operated for the sole purpose of liquidating real property as a single venture (with such powers of administration as are incidental thereto, including the acquisition, improvement, conservation, division, and sale of such property), distributing the proceeds therefrom in due course to or for the benefit of the beneficiaries, and discharging indebtedness secured by the trust property, and (3) has not made a return for the taxable year as an association.

Regulations 65, promulgated under the Revenue Act of 1924:

ART. 1502. *Association.*—Associations and joint-stock companies include associations, common-law trusts, and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the shareholders on the basis of the capital stock which each holds, or, where there is no capital stock, on the basis of the proportionate share or capital which each has or has invested in the business or property of the organization. A corporation which has ceased to exist in contemplation of law but

continues its business in corporate form is an association or corporation within the meaning of section 2, but if it continues its business in the form of a trust, it becomes subject to the provisions of section 219.

ART. 1504.[1] *Association distinguished from trust.*—Where trustees merely hold property for the collection of the income and its distribution among the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, and the beneficiaries have no control over the trust although their consent may be required for the filling of a vacancy among the trustees or for a modification of the terms of the trust, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by section 219 and by articles 341–347. If, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists within the meaning of section 2. Even in the absence of any control by the beneficiaries, where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the statute.

Article 1502 and Article 1504 of Regulations 69, promulgated under the Revenue Act of 1926, are substantially identical with Articles 1502–1504 of Regulations 65, *supra*.

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[1] As amended by T. D. 3748, IV–2 Cumulative Bulletin 7.

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OCT 11 1935

No. 17

In the Supreme Court of the United States

OCTOBER TERM, 1935

T. A. MORRISSEY AND JAMES M. O'BRIEN, TRUSTEES OF AN EXPRESS TRUST KNOWN AS WESTERN AVENUE GOLF CLUB, PETITIONERS

v.

GUY T. HELVERING, COMMISSIONER OF INTERNAL REVENUE.

ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT

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No. 17

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ON WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE NINTH CIRCUIT

BRIEF FOR THE RESPONDENT

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The memorandum opinion of the United States Board of Tax Appeals (R. I, 31–51) is unreported. The opinion of the Circuit Court of Appeals (R. I, 67–72) is reported in 74 F. (2d) 803.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered January 7, 1935 (R. I, 73). A petition

for rehearing was denied March 1, 1935 (R. I, 74). Petition for a writ of certiorari was filed April 1, 1935, and was granted May 13, 1935 (R. II, 41). The jurisdiction of this Court is invoked under Section 240 (a) of the Judicial Code as amended by the Act of February 13, 1925.

QUESTIONS PRESENTED

1. Whether the trust involved is an association within the meaning of Section 2 (a) (2) of the Revenue Acts of 1924 and 1926.

2. Whether Section 704 (a) of the Revenue Act of 1928 prevents the trust involved from being regarded as an association for the year 1924.[1]

STATUTES AND OTHER AUTHORITIES INVOLVED

The statutes and other authorities involved are set out in Appendix A, *infra*, pp. 35–46.

STATEMENT

The following facts are taken from the stipulation of facts (R. I, 22–31), from the Board's opinion (R. I, 31–51) and from the trust instrument (R. II, 1–37).

On October 4, 1921, T. A. Morrissey and James M. O'Brien executed a declaration of trust by which they declared that they held a certain parcel of real estate in Los Angeles, California, consisting of 155 acres in trust. (R. I, 33; R. II, 1.)

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[1] This question was not raised in the petition for writ of certiorari, but is discussed in the petitioner's brief on the merits.

The trust instrument directed that they should hold that property and any other property thereafter conveyed to them as trustees in trust to collect, receive, hold and distribute the net income thereof for the benefit of those holding certificates of beneficial interest. The trustees were also authorized to buy, sell, lease and mortgage real estate, to farm, to construct or acquire and operate golf courses, tennis courts, swimming pools, bowling alleys and club houses and stores, shops and cafes and other businesses in connection therewith. Broad powers of management were given to them in the exercise of these powers. (R. II, 1–14.)

The trust was to be called the "Western Avenue Golf Club" and was to exist for twenty-five years, unless the trustees themselves should elect to terminate it before that time. (R. II, 2, 31.)

The trustees were empowered to increase their number and to elect successor trustees by a majority vote. They were also authorized to appoint an advisory board, an executive committee and officers, but the appointment of the advisory board was not to limit the powers of the trustees. (R. II, 2–3, 11–12.)

Neither the trustees nor the directors, executive committee or officers were to be personally liable for any obligations of the trust, the trust fund being the sole source of reimbursement or payment. (R. II, 15–16.)

There were to be two thousand preferred shares of beneficial interest of a par value of $100 a share

and an equal number of common shares of no par value. The latter were subject to assessments. (R. II, 19, 25–26.)

The preferred certificate holders were entitled to a fixed dividend and the common certificate holders to such dividends as the trustees declared. (R. II, 19–20.)

The trust instrument provided that neither class of certificate holders should have any rights different from those of *cestui que trustent*. (R. II, 30.)

During the years 1921 and 1922 the trustees sold beneficial interests in the trust, paying $5,692.90 and $5,036.15 to salesmen in commissions on the sales. (R. I, 36.)

About 42 acres of the land constituting the trust corpus was subdivided into lots in December, 1921. Improvements were made and all of the lots were sold in 1922, 1923 and 1924. (R. I, 26.)

On that part of the property not subdivided, a golf course and club house were built in 1922. The club was open only to the beneficiaries and other members and their guests. Greens fees were charged and the dining room and golf supplies department were operated by concessionaires on a percentage basis. (R. I, 26–27.)

In July 1923 the land comprising the golf course, with other improvements, was conveyed to a corporation known as Western Avenue Golf Club, Incorporated, in exchange for its stock.

Thereafter until January 12, 1924, the trust operated it under a lease. (R. I. 39–40.)

Collections of installment payments on the contracts for the sale of lots were made during 1921 to 1926 by a bank as agent. Since January 12, 1924, the trust's activities have consisted of collections on lots, collection of interest payments on bank balances and dividends on stock, receipt of assignment fees in assignment of lot purchase contracts by holders, execution of conveyances and the distribution of moneys. (R. I, 41–42.)

During the years 1922 to 1926, inclusive, the trustees owned from 15.8% to 42.4% of the beneficial interest. (R. I, 43.) From 275 to 920 persons held interests at various times. (R. I, 31.)

The trust filed returns as a trust for the years 1921 to 1926, inclusive. The Commissioner determined that it was an association and asserted deficiencies. The Board sustained the Commissioner's determination for the years 1924, 1925 and 1926,[2] which are the taxable years here involved, and the Circuit Court of Appeals affirmed the Board's decision.

SUMMARY OF ARGUMENT

The decisions of this Court establish that some organizations which are trusts in form may be treated as associations for Federal tax purposes and taxed as corporations, and that a trust may be

[2] There were other issues involved before the Board which are not before this Court.

an association regardless of whether the beneficiaries have control. The decisions of the Circuit Courts of Appeals are to the same effect, although they differ as to what is the proper test.

Since associations are by the statute assimilated to corporations, the problem is to determine what features associations have in common with corporations which led to this classification. The question is complicated by the fact that all associations have features which are common to those trusts separately taxed under Section 219, and the need for drawing a distinction between them. We think that the distinction between associations and the trusts taxed under Section 219 is the distinction between business trusts on the one side and on the other trusts which are engaged merely in collecting the income and conserving the property against the day when it is to be distributed to the beneficiaries. We submit that Congress intended that all business trusts should be taxed as associations, and hence that the "doing business" test which is emphasized by many decisions is the single criterion on which this case should depend.

Some courts have held that the activities in which the organization is engaged are not the sole test, but that the qualities and characteristics of the organization must likewise be examined in order to determine whether classification as a corporation is justified. However, the courts holding this view differ widely in the relative importance

to be given to matters of substance and matters of form. In some decisions such incidental features as seals, officers, meetings, etc., are magnified in importance, while other cases hold that the necessary similitude is to be found if the organization has the substantial qualities of a corporation, such as centralized control, continuity, and limited liability. If it is necessary to have regard for anything more than the activities of the organization and doing business is not the sole test, we think that an organization which does business and enjoys the substantial advantages of centralized control, continuity, and limited liability is an association within the meaning of the statute. Applying either test, the trust here involved is properly classified as an association.

It is our position that the decisions of this Court establish that a trust is an association, when it is engaged in doing business.

Treasury regulations to this effect were promulgated under the Revenue Acts of 1924 and 1926 after pertinent decisions of this Court were rendered.

Section 704 (a) of the Revenue Act of 1924 has no application to the case, since the regulations were changed to eliminate the necessity of beneficiary control prior to the time that the trust filed its return as a trust for 1924.

No double taxation is involved in taxing the trust as a corporation even if it receives dividends from

another corporation. These dividends would not be taxed to the association under the statutes here involved, and when distributed to individual certificate holders as its dividends would only be subject to surtax in their hands, just as the earnings of any corporation are subject to a corporate tax and then to surtax when distributed to individual stockholders.

ARGUMENT

I

THE WESTERN AVENUE GOLF CLUB WAS AN ASSOCIATION WITHIN THE MEANING OF SECTION 2 (A) (2) OF THE REVENUE ACTS OF 1924 AND 1926

The chief question is whether the trust involved is an association within the meaning of Section 2 (a) (2) of the Revenue Acts of 1924 and 1926 and hence is to be taxed as a corporation, or is a pure trust which by virtue of Section 219 of those Acts is taxed as an individual.

The statutes involved do not define the term "association" or provide a rule for distinguishing between trusts which are to be taxed as trusts and those which were to be treated as associations, but they do indicate very clearly that the trusts to be treated as pure trusts under Section 219 are those organized and engaged solely to hold or conserve property.

That all organizations which are trusts in form are not to be so treated for tax purposes is settled

by the decisions of this Court in *Crocker* v. *Malley*, 249 U. S. 223, and *Hecht* v. *Malley*, 265 U. S. 144, although in neither case was an all-embracing definition of the word "association" adopted.

The case of *Crocker* v. *Malley* involved taxes imposed under the Revenue Act of 1913 upon the income of "every corporation, joint-stock company or association". That statute, however, did not contain any provisions indicating the classes of trusts[1] to be taxed as individuals such as are incorporated in Section 219 of the Revenue Acts of 1924 and 1926, *infra*. The trust in that case had been formed by a Maine corporation which had been engaged in the manufacture of paper. Seven of the mills which it owned and operated in Massachusetts had been transferred to a Massachusetts corporation in exchange for stock and the eighth had been leased to the latter on a long term lease. The Maine corporation transferred the fee of the eighth mill to certain individuals in trust, left the stock of the Massachusetts corporation in their hands for the time being, though it was possible that the Maine company shareholders might have demanded it, and was dissolved.

The declaration of trust directed the trustees to hold the real estate and other property received, to convert it into money and distribute it to the holders of beneficial interest in the trust. The trust was stated to be for the benefit of the eight share-

[1] See Section II B and D.

holders of the Maine corporation and its purpose that of permitting dissolution before final distribution of assets; although the trustees had power to acquire other property. The beneficiaries' consent was required in filling vacancies among the trustees and in providing for the compensation of the trustees and in modifying the trust. The trust was known as "The Massachusetts Realty Trust".

This Court held that the trust in question was not an association. In so holding, the Court recognized that the case was not necessarily controlled by the fact that the trust was regarded as a trust in Massachusetts, where organized, but concluded that the trust was a pure trust because the beneficiaries had no control. The Court, however, was clearly influenced in its decision by the use of the phrase "joint-stock companies or associations" in the statute there involved and by the fact that to have held the trust a corporation would have resulted in a double tax on corporate dividends, since the corporation paying them was taxed on its earnings and the statute there involved taxed a corporation on dividends received from other corporations.

The trust agreement involved in that case with modifications and two other Massachusetts real estate trusts were before this Court in *Hecht* v. *Malley*, 265 U. S. 144, *supra*, where the question was whether they were subject to capital stock tax imposed by Section 1000 of the Revenue Act of 1918 and also to another excise tax imposed on cor-

porations by the Revenue Act of 1916. Under the Revenue Act of 1918, as under the Revenue Act of 1924, the term "corporation" was defined to include associations instead of the tax being imposed in terms "corporations, joint-stock companies or associations" as under the 1913 Act, and the same definition was made applicable to the capital stock tax and the income tax.

The Court determined that the *Crocker* trust had been modified so as to transfer the assets of the business to the trust and authorize the trustees to carry on business and to enable the certificate holders to remove any trustee. It held that regardless of control by the beneficiaries, that trust, as well as the other trusts involved, were associations under the Revenue Act of 1918.

In doing so the Court rejected the argument that the *Crocker case, supra,* had conclusively determined that a Massachusetts trust could not be an association without beneficiary control, and said (pp. 160–161):

> This opinion is based primarily upon the view that the Income Tax Act, considering its purpose, did not show a clear intention to impose upon the trustees as an "association" a double liability in reference to the dividends on stock in the corporation that itself paid an income tax, when considered as "trustees" they were by another provision of the Act exempt from such payment. And the language used *arguendo* in reaching this

conclusion that the trustees could not be deemed an association unless all trustees with discretionary powers are such, and that there was no ground for grouping together the beneficiaries and trustees in order to turn them into an association—is to be read in the light of the trust agreement there involved, under which the trustees were, in substance, merely holding property for the collection of the income and its distribution among the beneficiaries, and were not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business. *Zonne* v. *Minneapolis Syndicate,* 220 U. S. 187, 190. And see *Smith* v. *Anderson,* L. R., 15 Ch. Div. 247.

It results that *Crocker* v. *Malley* is not an authority for the broad proposition that under an Act imposing an excise tax upon the privilege of carrying on a business, a Massachusetts Trust engaged in the carrying on of business in a quasi-corporate form, in which the trustees have similar or greater powers than the directors in a corporation, is not an "association" within the meaning of its provisions.

We conclude, therefore, that when the nature of the three trusts here involved is considered, as the petitioners are not merely trustees for collecting funds and paying them over, but are associated together in much the same manner as the directors in a corporation for the purpose of carrying on business enterprises, the trusts are to be

deemed associations within the meaning of the Act of 1918; this being true independently of the large measure of control exercised by the beneficiaries in the *Hecht* and *Haymarket* cases, which much exceeds that exercised by the beneficiaries under the Wachusett Trust. We do not believe that it was intended that organizations of this character—described as "associations" by the Massachusetts statutes and subject to duties and liabilities as such—should be exempt from the excise tax on the privilege of carrying on their business merely because such a slight measure of control may be vested in the beneficiaries that they might be deemed strict trusts within the rule established by the Massachusetts courts.

It is our position that the decision in *Hecht* v. *Malley, supra,* determined that a trust under which a combination of persons were doing business would be an association irrespective of beneficiary control and, in the alternative, that if that decision made the further requirement that the trust must resemble a corporation, this requirement was simply that the trust should have the attributes of a corporation such as centralized control, continuity of existence, and limited liability, regardless of forms used in effecting them.

The courts and the regulations of the Treasury Department have accepted the view that beneficiary control is no longer a requisite, except in so far as the question may be affected by Section 704

(a) of the Revenue Act of 1928, an issue discussed in Point II.

We do not believe that the petitioners seriously argue otherwise or that the point requires extended consideration here. The petitioners do suggest that the decision in *Crocker* v. *Malley, supra,* is entitled to greater weight than *Hecht* v. *Malley, supra,* because the former was an income-tax case and the latter a capital-stock case. But Section 2 of the Revenue Act of 1918 involved in *Hecht* v. *Malley, supra,* and of the Revenue Acts of 1924 and 1926, *infra,* here involved, give a single definition of the word "corporation" to be used throughout the statute in imposing both taxes, so that this contention is without merit. The courts generally have considered that *Hecht* v. *Malley* controlled. See *Little Four Oil & Gas Co.* v. *Lewellyn,* 35 F. (2d) 149 (C. C. A. 3d), certiorari denied, 280 U. S. 613; *Gray* v. *Hopkins,* 68 F. (2d) 561 (C. C. A. 5th; certiorari denied, 292 U. S. 643; *Ittleson* v. *Anderson,* 67 F. (2d) 323 (C. C. A. 2d); *Dunbar* v. *Commissioner,* 65 F. (2d) 447 (C. C. A. 1st); *Twin Bell Oil Syndicate* v. *Helvering,* 70 F. (2d) 402 (C. C. A. 9th), reversed on other grounds, 293 U. S. 312.

The regulations issued by the Treasury Department likewise have assumed that *Hecht* v. *Malley, supra,* controlled in income-tax cases. Following the decision in *Hecht* v. *Malley, supra,* in May 1924, the Treasury Department published the decision as a Treasury decision, and on June 7, 1924, issued T. D. 3598, III–1 Cumulative Bulletin 489, which

defined the term "association" for capital-stock tax purposes to include operating trusts of the Massachusetts type, regardless of beneficiary control. By I. T. 2061, published August 11, 1924, III–2 Cumulative Bulletin 5 (for date issued see G. C. M. 6417, VIII–1 Cumulative Bulletin 152), this ruling was made applicable to income taxes imposed under the Revenue Act of 1924 and the definition appeared in Regulations 65, promulgated under the Revenue Act of 1924, when they were issued in October, 1924. See Article 1504, *infra*.

This regulation was amended by T. D. 3748, IV–2 Cumulative Bulletin 7, *infra*, so as to provide, *inter alia*, that a trust in which the beneficiaries have control should be regarded as an association but that even in the absence of control, where the trustees are not restricted to the mere collection of funds and their distribution but are "associated together with similar or greater powers than that of directors of a corporatio for the purpose of carrying on some business en rise", the trust should be regarded as an association. On the other hand, trusts in which the trustees are merely holding property and collecting income for distribution, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of business, the trust is regarded as a pure trust and not an association.[4]

[4] It will be noted that under the regulations a trust in which the beneficiaries do control is still treated as an association on the basis of the test in *Crocker* v. *Malley*, *supra*.

Similar regulations were promulgated under the Revenue Acts of 1926, 1928 and 1932 (see Articles 1502 and 1504 of Regulations 69 and Articles 1312 and 1314 of Regulations 74 and 77, *infra*), except that in Article 1314 of Regulations 77 all reference to control by beneficiaries was eliminated. But under all of these regulations the test of engaging in business was made the paramount test, since even without beneficiary control a trust might be classified as an association if it engaged in business.

We submit that the regulations promulgated under the Revenue Acts of 1924 and 1926 are the basic regulations in this case, although for reasons we shall subsequently point out the regulations themselves may require interpretation as applied to certain situations not specifically covered by them. There is clearly no merit to the petitioners' argument that the regulations promulgated under the Revenue Acts of 1918 and 1921 control under the Revenue Acts of 1924 and 1926 because Congress reenacted the same statutory definition of corporations in the Revenue Act of 1924, after the regulations had been continued in effect for an extended period. To hold otherwise would be to say that the Commissioner cannot issue a changed regulation unless statutory provisions are changed, even when this Court has rendered a decision finding its interpretation inconsistent with the law.

See S. M. 4104, IV–2 Cumulative Bulletin 8. But trusts in which the beneficiaries have no control are regarded as associations if there is a combination of persons involved and the trust is doing business.

While we readily concede that an unchanged regulation may acquire the force and effect of law through legislative approval (*McCaughn* v. *Hershey Chocolate Co.*, 283 U. S. 488; *Brewster* v. *Gage*, 280 U. S. 327; *Helvering* v. *Bliss*, 293 U. S. 144), we know of no decision which holds that the Commissioner may not issue a new regulation under a new law. Amended regulations under the same law are often given effect even as to transactions fully consummated (*Murphy Oil Co.* v. *Burnet*, 287 U. S. 299, 303–304; *Burnet* v. *S. & L. Bldg. Corp.*, 288 U. S. 406), and Section 605 of the Revenue Act of 1928 implies that regulations may be applied either retroactively or not, as the Secretary directs. See also Section 1008 of the Revenue Act of 1924 and Section 1108 of the Revenue Act of 1926.

Moreover, as to the particular statute here involved, the courts have consistently recognized that the regulations governing the year 1924 are Articles 1502 and 1504 of Regulations 65, promulgated under the Revenue Act of 1924 as amended. *Gray* v. *Hopkins, supra; Commissioner* v. *Neal*, 65 F. (2d) 761 (C. C. A. 1st), certiorari denied, 290 U. S. 675; *Dunbar* v. *Commissioner, supra; Tyson* v. *Commissioner*, 68 F. (2d) 584 (C. C. A. 7th), certiorari denied, 292 U. S. 657. See also brief of *amicus curiae*.

The regulations perhaps suggest that, in addition to the requirement for doing business, there

must be a combination of persons in management, and the rulings have generally been based on the theory of the necessity for beneficiary participation in management in cases involving a single trustee. See I. T. 2572, X–1 Cumulative Bulletin 200; G. C. M. 2405, VI–2 Cumulative Bulletin 10; S. M. 5382, V–1 Cumulative Bulletin 11. See also *Trust No. 5833, Security First Nat'l Bank* v. *Welch*, 54 F. (2d) 323, certiorari denied, 286 U. S. 544.

In *Crocker* v. *Malley, supra,* it was held that the trustees and beneficiaries together did not furnish the combination of persons necessary to an association but this Court apparently held otherwise in *Hecht* v. *Malley, supra.*

In this case there was more than one trustee engaged in management, but we think it desirable to state the Government's position that the necessary combination may exist without that factor. See Article 801–3 of Regulations 86, *infra,* promulgated under the Revenue Act of 1934, and see Section 704 (b) of the Revenue Act of 1928, *infra.* Every trust involves the combination of persons necessary to an association, regardless of whether they be combined in management. Even in a case where a single trustee is managing the business, it is his management and the capital of the beneficiary or beneficiaries that produces the profit. See *Ittleson* v. *Anderson, supra,* in which the following is stated:

> Usually there are a number of trustees and of beneficiaries in a business trust, but there is no reason to say that every business trust must have more than one trustee and more than one beneficiary at all times.

The situation is not unlike that in a certain type of limited partnerships which are treated as associations. See Article 1506 of Regulations 65 and 69. There is also an analogy to groups doing a reciprocal or similar insurance business through an attorney-in-fact which have been held to be associations. *Harris* v. *United States,* 51 F. (2d) 382 (S. D. Tex.). See also *Pickering* v. *Alyea-Nichols Co.,* 21 F. (2d) 501 (C. C. A. 7th), certiorari denied, 276 U. S. 617.

We submit, therefore, that the doing business test is the essential test under the decision of this Court in *Hecht* v. *Malley, supra* and under the regulations.

Some of the Circuit Courts of Appeals, however, have considered that *Hecht* v. *Malley, supra,* also requires that there be external resemblances to a corporation.

It is true that in that case the Court referred to a dictionary definition of an association as "a body of persons united without a charter, but upon the methods and forms used by incorporated bodies for the prosecution of some business enterprise", and that it designated the trusts there involved as "quasi-corporate" organizations, but the decision was finally made to rest upon whether the trustees

were associated together in much the same manner as directors of a corporation for the purpose of carrying on a business enterprise. Each trust was tested under this rule and found to be an association.

The Circuit Courts of Appeals for the Second and Third Circuits have consistently relied upon the business test as conclusive and that was the view of the Circuit Court of Appeals for the Ninth Circuit until its recent decision in *Commissioner* v. *Combs,* 76 F. (2d) 682, now pending before this Court on petition for a writ of certiorari, No. 238, October Term, 1935. The Circuit Court of Appeals for the First, Fifth, Seventh and Tenth Circuits have in general insisted on the test of external resemblance, although the decisions of the First and Seventh Circuits are not wholly consistent. A list of these decisions will be found in Appendix B, *infra.* No decisions have been found in the Circuit Courts of Appeals for the Fourth, Sixth and Eighth Circuits, or in the Court of Appeals for the District of Columbia, except *Burnet* v. *Burns,* 63 F. (2d) 313 (C. C. A. 8th), which is inconclusive on this question. The Circuit Court of Appeals for the First Circuit commented on the conflict of decisions in *Coleman-Gilbert Associates* v. *Commissioner,* 76 F. (2d) 191, now pending in this Court on petition for writ of certiorari, Nos. 78 and 79, October Term, 1935.

We believe that an analysis of the cases in which resemblances to a corporation have been weighed

and relied upon will show how impossible it is to make them the test. In some cases certificates of stock or a seal or formal meetings of the trustees like directors' meetings will be regarded as important, and in others not so important. For example, compare *Sears, Roebuck & Co. Employees' Savings, etc.* v. *Commissioner,* 45 F. (2d) 506 (C. C. A. 7th), where there were no certificates, and the decisions of the same court in *Tyson* v. *Commissioner, supra,* and *Reinecke* v. *Kaempfer,* 72 F. (2d) 469, certiorari denied, 294 U. S. 708, with *Commissioner* v. *Guitar Trust Estate,* 72 F. (2d) 544 (C. C. A. 5th).

We submit that in order for the various Circuit Courts of Appeals, the District Courts and the Board to achieve some degree of uniformity in their decisions, either the business test must be considered conclusive in itself or conclusive where there are some or all of the elements of centralized control, limited liability and continuity of the business regardless of death or transfers of interest and that it is not important whether the trust has certificates of stock or other external features of a corporation. See Article 801–3 of Regulations 86, *infra.*

The first alternative has the advantage of simplicity and is not inconsistent with the statute or regulations or with what this Court said in *Hecht* v. *Malley, supra.*

It should be remembered that the ordinary trust *per se* has certain corporate attributes in that ordi-

narily there is no personal liability of trustees or beneficiaries and the beneficiaries are free to dispose of their beneficial interests, regardless of whether they are represented by shares.

The enumeration of trusts in the subdivisions of Section 219 (a) of the Revenue Acts of 1924 and 1926 suggests that in enacting those provisions Congress had in mind testamentary trusts and other trusts created simply to conserve assets and collect income and pay it over or accumulate it for future distribution.

Articles 801–2 and 801–3 of Regulations 86, promulgated under the Revenue Act of 1934, *infra*, adopt this view. These regulations draw a distinction between a trust created by will or otherwise for the purpose of taking title to property and conserving it, engaging in only such activities as are required, and a trust designed to afford a medium whereby a profit-seeking activity may be carried out with some of the advantages and none of the disadvantages of a corporation. Article 801–3 points out the benefits of such an arrangement as follows:

> By means of such a trust the disadvantages of an ordinary partnership are avoided, and the trust form affords the advantages of unity of management and continuity of existence which are characteristic of both associations and corporations. This trust form also affords the advantages of

capacity, as a unit, to acquire, hold, and dispose of property and the ability to sue and be sued by strangers or members, which are characteristic of a corporation; and also frequently affords the limitation of liability and other advantages characteristic of a corporation. These advantages which the trust form provides are frequently referred to as resemblance to the general form, mode of procedure, or effectiveness in action, of an association or a corporation, or as "quasi-corporate form." The effectiveness in action in the case of a trust or of a corporation does not depend upon technical arrangements or devices such as the appointment or election of a president, secretary, treasurer, or other "officer," the use of a "seal," the issuance of certificates to the beneficiaries, the holding of meetings by managers or beneficiaries, the use of a "charter" or "by-laws," the existence of "control" by the beneficiaries over the affairs of the organization, or upon other minor elements. They serve to emphasize the fact that an organization possessing them should be treated as a corporation, but they are not essential to such classification, for the fundamental benefits enjoyed by a corporation, as outlined above, are attained, in the case of a trust, by the use of the trust form itself.

We believe that these regulations, which do not so much depart from previous regulations as they simplify and clarify them, should be recognized as

stating the correct principles under the earlier statutes. The statutory provision was not changed. See Section 801 of the Revenue Act of 1934.

But if it is considered necessary that there be corporate attributes, we believe that the attributes which are important are those of substance and not of form, as in other fields of taxation. *United States* v. *Phellis*, 257 U. S. 156; *Weiss* v. *Stearn*, 265 U. S. 242; *Labrot* v. *Burnet*, 57 F. (2d) 413 (App. D. C.).

We submit that externals were not considered as important in *Hecht* v. *Malley, supra*. In that case this Court quoted its previous decision in *Flint* v. *Stone Tracy Co.*, 220 U. S. 107, where the Court, in sustaining an excise tax measured by income which was imposed only on corporations, stated that the tax was imposed on the doing of business with the advantages which lay in the peculiarities of corporations or joint-stock associations.

This language suggests that a trust having the substantial qualities of a corporation, such as centralized control, continuity and limited liability, should be taxed as one. Somewhat the same thought is expressed in *Reinecke* v. *Kaempfer, supra*, where the court said (pp. 470–471):

> As we pointed out in *Sears, Roebuck, etc.*, v. *Commissioner*, 45 F. (2d) 506, there are various kinds of corporations, some with and some without shares of stock; and some for and others not for pecuniary profit. And it was there held that shares of stock, or the

> equivalent, and assignable interests of beneficiaries were not essential to constitute a taxable association under the statute. The entity there involved was without shares of capital stock and without assignable interests, but it was held to be a taxable association under the act.
>
> We are satisfied that the similitude referred to is not in those essentials which distinctly stamp the entity as a corporation, but rather in the business carried on and the manner of its transaction. This entity carried on its business in substantially the same way that a corporation would have carried it on. It regularly bought and sold merchandise for the purpose of realizing profit thereon; it constituted the persons to carry on the business, and even made provision for exemption of the trustees from personal liability for trust obligations, much as in the case of business corporations.

The facts in the present case are such that the trust satisfies the doing-business test and, if more be required, it has the centralized control, continuity and limited liability of a corporation.

The trust in this case was a voluntary association of individuals who acquired 155 acres of land in Los Angeles with a view to subdividing part of it into lots and selling them at a profit and developing a golf course on the remainder. (R. I, 47.) It proceeded to accomplish those purposes. It subdivided the property, made street and other improvements and disposed of the lots at a substantial

profit during the years 1921 to 1923. It also developed the golf course as a profit-making enterprise.

The petitioners argue that because all of the lots had been sold before 1924, and the golf course was not operated by the trust after January 12, 1924, the trust was not doing business during the years 1924, 1925 and 1926, but was merely in process of liquidation.

The petitioners thus fail to distinguish between cases involving a trust which is organized for the purpose of liquidation (*White* v. *Hornblower*, 27 F. (2d) 777 (C. C. A. 1st); *Commissioner* v. *Atherton*, 50 F. (2d) 740 (C. C. A. 9th); *Blair* v. *Wilson Syndicate Trust*, 39 F. (2d) 43 (C. C. A. 5th); *Fisk* v. *United States*, 60 F. (2d) 665 (Mass.); *Commissioner* v. *Morriss R. Co. Trust No. 2*, 68 F. (2d) 648 (C. C. A. 7th); *Willis* v. *Commissioner*, 58 F. (2d) 121 (C. C. A. 9th)) and cases in which a trust organized for profit has carried out most of the activities for which it was organized except the collection of its profits.

This distinction is emphasized in *Sloan* v. *Commissioner*, 63 F. (2d) 666 (C. C. A. 9th), where the trust was organized for the purpose of leasing, mortgaging and selling lots in a subdivision but had ceased to transact any business other than the collection and distribution of installment payments. The court held that it was not to be considered as a trust merely because all of its lots had been sold.

This Court has recognized that less activity is required to hold that a corporation which was organized for profit is doing business than one organized merely to hold property and collect income. *Flint* v. *Stone Tracy Co., supra; Zonne* v. *Minneapolis Syndicate,* 220 U. S. 187; *McCoach* v. *Minehill Railway Co.,* 228 U. S. 295; *United States* v. *Emery,* 237 U. S. 28; *Von Baumbach* v. *Sargent Land Co.,* 242 U. S. 503; *Edwards* v. *Chile Copper Co.,* 270 U. S. 452. See also *Stanley Securities Co.* v. *United States,* 38 F. (2d) 907 (C. Cls.), certiorari denied, 282 U. S. 845.

The petitioners apparently consider that only a trust engaged in a merchandising business may be said to be engaged in business, and that a trust operating real estate may not. But many trusts engaged in real estate subdivision or management have been held to be associations. *Hecht* v. *Malley, supra; Sloan* v. *Commissioner, supra; Commissioner* v. *Neal,* 65 F. (2d) 761 (C. C. A. 1st), certiorari denied, 290 U. S. 675; *Tyson* v. *Commissioner, supra; Swanson* v. *Commissioner,* 76 F. (2d) 651 (C. C. A. 7th), now pending before this Court on petition for a writ of certiorari, No. 108, October Term, 1935.

If it is also required that the trust have centralized control, continuity and limited liability, or one or more of them, all of those elements are present in this case.

The trustees were given exceedingly broad powers of management and were authorized to appoint an advisory board and executive officers to act with them. (R. II, 4–13.) During the years involved in this case the trustees acted for between 275 and 920 persons. (R. I, 31.)

There was also no liability against the directors, advisory committee or officers for debts incurred by the corporation. (R. II, 15–16.) The beneficiaries holding common shares were liable for assessments but only to the extent that stockholders of a California corporation are liable. (R. II, 25–26.)

The trust was to last for twenty-five years, unless the trustees elected to terminate it before that time (R. II, 2, 31), and the beneficiaries could alienate their interests which were in the form of certificates. (R. II, 19–21, 25–26, 30.)

Accordingly, the trust had centralized control, limited liability and continuity, which are peculiar to a corporation.

We think that is all that can be required under any test. We point out in passing, however, that the trust here involved had many external resemblances to a corporation, so that even under the petitioners' construction of the statute there is justification for holding that the trust was an association under Section 2 (a) (2) of the Revenue Acts of 1924 and 1926.

The petitioners claim (Br. 20–21) that such a result would be contrary to the decision of this Court in *Senior* v. *Braden*, decided May 20, 1935, which involved an Ohio property tax. The question there was whether cetrificates of beneficial interest in certain trusts (each of which owned only one piece of real estate) represented an interest in the land itself, which could not be reached by the tax because situated outside of Ohio, or personal property. The Court pointed out that each trustee held only one piece of land and was free from control by the beneficiaries, citing *Hecht* v. *Malley, supra.*

That case was not cited as decisive of the questions here involved, but apparently as an example of one species of trusts considered by this Court to be an association. Indeed, in *Hecht* v. *Malley*, it is specifically stated:

> What other form of "associations," if any, it includes, we need not, and do not, determine.

In any event, a decision as to what constitutes an association for Federal tax purposes is not controlled by decisions under state laws. *Crocker* v. *Malley, supra; Burk-Waggoner Oil Assn.* v. *Hopkins*, 269 U. S. 110.

The petitioners also argue (Br. 15) that to classify the trust involved in this case as an association will result in the same kind of double taxation that the Court found objectionable in *Crocker* v. *Malley, supra.*

This position is wholly untenable. If the trust in this case is held to be an association, it will be taxed as a corporation at the regular rates imposed by Section 230 of the Revenue Acts of 1924 and 1926; namely, 12½% for 1924, 13% for 1925 and 13½% for 1926. It will not, however, be taxed on any dividends. Section 234 (a) (6) of the Revenue Acts of 1924 and 1926. Any distributions that it makes will be regarded as dividends and if paid to individuals will be subject to surtax but not to normal tax. See Section 216 (a) of the Revenue Acts of 1924 and 1926. If paid to a corporate beneficiary, they will not be taxed at all. Section 234 (a) (6) of the Revenue Acts of 1924 and 1926. Hence the dividends which the trust receives from other corporations and distributes to beneficiaries will not be taxed to it at all but will be subject to surtax in the hands of individual beneficiaries. Hence the corporate dividends are not taxed twice.

There is no double taxation involved in an individual paying a surtax on dividends received from a corporation which had been taxed on its earnings. *Hellmich* v. *Hellman,* 276 U. S. 233.

The situation in *Crocker* v. *Malley, supra,* was very different. As previously pointed out, under that Act a corporation was subject to tax at regular corporate rates on dividends received from another corporation, so that if the trust had been held to be an association, it would have been subject to the same kind and rate of tax on the earnings represented by any corporate dividends it received

that the corporation declaring the dividends had already paid. That situation does not arise here.

II

SECTION 704 (A) OF THE REVENUE ACT OF 1928 HAS NO APPLICATION TO THIS CASE

The petitioners argue that the trust should be treated as a pure trust for the year 1924 by virtue of Section 704 (a) of the Revenue Act of 1928.

This issue was not raised in the petition for a writ of certiorari, and we do not believe that the Court is required to pass upon it. *Webster Co.* v. *Splitdorf Co.*, 264 U. S. 463; *Gunning* v. *Cooley*, 281 U. S. 90; *Alice State Bank* v. *Houston Pasture Co.*, 247 U. S. 240.

But if the Court should consider the question, we think it clear that Section 704 (a) has no application.

That section provides in substance that where a taxpayer has filed a return for any year prior to the year 1925, it shall be taxed as a trust and not as a corporation (1) if it was regarded as a trust under regulations in effect when the return was filed, or (2) if it was regarded as a trust under any ruling of the Commissioner which had not been reversed or revoked prior to the time the return was made.

The purpose of this legislation was to permit the test of liability for taxable years prior to 1925 to be governed by regulations and rulings in effect at the time the return was made, provided a return

was filed as a trust. *Gray* v. *Hopkins*, 68 F. (2d) 561 (C. C. A. 5th), certiorari denied, 292 U. S. 643; *Sloan* v. *Commissioner*, 63 F. (2d) 666 (C. C. A. 9th); S. Rep. No. 960, 70th Cong., 1st Sess., pp. 44–45.

Under Article 1502 and Article 1504 of Regulations 62, *infra*, promulgated under the Revenue Act of 1921, it was generally assumed that a trust in which the beneficiaries had no control should be regarded as a pure trust, although the regulations are not wholly clear. *Sloan* v. *Commissioner, supra.* Hence if that regulation or rulings to the same effect had remained in force until the petitioners filed a return for 1924 as a trust, the trust should be treated as a pure trust and not as an association for the year 1924, regardless of the disposition made of the later years. It was on that basis that the Board held that the trust was a pure trust for the years 1921, 1922 and 1923. (R. I, 46–47.)

But regulations and rulings to that effect did not remain in force until the return for 1924 was filed.

The record does not show when the return for 1924 was filed, but it was not due until March 15, 1925, and could not have been filed prior to January 1, 1925.

Before either date this Court had, on May 12, 1924, decided the case of *Hecht* v. *Malley*, 265 U. S. 144, which held that a trust might be regarded as an association regardless of beneficiary control. On June 7, 1924, the Secretary of the Treasury promulgated T. D. 3598, III–1 Cumulative Bulletin

489, amending the capital stock regulations so as to omit reference to beneficiary control and to provide that operating trusts in which the trustees were not restricted to the collection of funds but were associated together in much the same manner as directors of a corporation in carrying on a business enterprise should be treated as associations.

On July 9, 1924, the Solicitor of Internal Revenue in S. M. 2291 ruled that the decision was applicable under the income-tax provisions of the Revenue Act of 1924 and this decision was published August 18, 1924, III–2 Cumulative Bulletin 6. Another ruling to the same effect, I. T. 2061, III–2 Cumulative Bulletin 5, was published August 11, 1924.

On October 6, 1924, Regulations 65 were promulgated under the Revenue Act of 1924, and Article 1504, *infra*, contained provisions similar to T. D. 3598, *infra*.

Under Article 1700 of those Regulations all rulings inconsistent therewith were revoked.

It is not necessary to consider the subsequent amendment of Articles 1502 and 1504 by T. D. 3748 and T. D. 3749, promulgated August 31, 1925, *infra*, for the reason that under those articles prior to the amendment an operating trust engaged in business would be taxed as an association, irrespective of beneficiary control.

It is clear, therefore, that there were no rulings or regulations in effect when the 1924 return was filed under which this trust would have been treated

as a pure trust because of the lack of beneficiary control. In G. C. M. 6417, VIII–1 Cumulative Bulletin 152, it was stated that August 11, 1924, should be regarded as the effective date of the change. See also *Van Cleave Trust* v. *Commissioner*, 18 B. T. A. 486.

The Circuit Courts of Appeals and the Board have held that other trusts filing returns for the year 1924 do not secure any relief under Section 704 (a) under such circumstances. *Gray* v. *Hopkins, supra; Commissioner* v. *Neal, supra; Sloan* v. *Commissioner, supra; Van Cleave Trust* v. *Commissioner, supra; Leszczynski* v. *Commissioner*, 29 B. T. A. 551; *Dutton* v. *Commissioner*, 18 B. T. A. 1151. See also *Landreth* v. *Commissioner*, 15 B. T. A. 655; *Dunbar* v. *Commissioner*, 65 F. (2d) 447 (C. C. A. 1st).

We submit, therefore, that Section 704 (a) has no application to this case.

CONCLUSION

The decision of the Circuit Court of Appeals should be affirmed.

Respectfully submitted.

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OCTOBER, 1935.

APPENDIX "A"

Revenue Act of 1924, c. 234, 43 Stat. 253:

SEC. 2. (a) When used in this Act—

* * * * *

(2) The term "corporation" includes associations, joint-stock companies, and insurance companies.

* * * * *

(U. S. C., Title 26, Sec. 1262.)

SEC. 210. (a) In lieu of the tax imposed by section 210 of the Revenue Act of 1921, there shall be levied, collected, and paid for each taxable year upon the net income of every individual (except as provided in subdivision (b) of this section) a normal tax of 6 per centum of the amount of the net income in excess of the credits provided in section 216, except that in the case of a citizen or resident of the United States the rate upon the first $4,000 of such excess amount shall be 2 per centum, and upon the next $4,000 of such excess amount shall be 4 per centum;

* * * * *

(U. S. C., Title 26, Sec. 951.)

SEC. 211. (a) In lieu of the tax imposed by section 211 of the Revenue Act of 1921, but in addition to the normal tax imposed by section 210 of this Act, there shall be levied, collected, and paid for each taxable year upon the net income of every individual a surtax as follows:

* * * * *

(U. S. C., Title 26, Sec. 952.)

SEC. 212. (a) In the case of an individual the term "net income" means the gross in-

come as defined in section 213, less the deductions allowed by sections 214 and 206.

* * * * *

(U. S. C., Title 26, Sec 53.)

SEC. 219. (a) The tax imposed by Parts I and II of this title shall apply to the income of estates or of any kind of property held in trust, including—

(1) Income accumulated in trust for the benefit of unborn or unascertained persons or persons with contingent interests, and income accumulated or held for future distribution under the terms of the will or trust;

(2) Income which is to be distributed currently by the fiduciary to the beneficiaries, and income collected by a guardian of an infant which is to be held or distributed as the court may direct;

(3) Income received by estates of deceased persons during the period of administration or settlement of the estate; and

(4) Income which, in the discretion of the fiduciary, may be either distributed to the beneficiaries or accumulated.

(b) Except as otherwise provided in subdivisions (g) and (h), the tax shall be computed upon the net income of the estate or trust, and shall be paid by the fiduciary. The net income of the estate or trust shall be computed in the same manner and on the same basis as provided in section 212, except that—

* * * * *

(U. S. C., Title 26, Sec. 960.)

(2) There shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is to be distributed currently by the fiduciary to the beneficiaries, and the amount of the income collected by a

guardian of an infant which is to be held or distributed as the court may direct, but the amount so allowed as a deduction shall be included in computing the net income of the beneficiaries whether distributed to them or not. Any amount allowed as a deduction under this paragraph shall not be allowed as a deduction under paragraph (3) in the same or any succeeding taxable year;

* * * * *

(3) In the case of income received by estates of deceased persons during the period of administration or settlement of the estate, and in the case of income which, in the discretion of the fiduciary, may be either distributed to the beneficiary or accumulated, there shall be allowed as an additional deduction in computing the net income of the estate or trust the amount of the income of the estate or trust for its taxable year which is properly paid or credited during such year to any legatee, heir, or beneficiary, but the amount so allowed as a deduction shall be included in computing the net income of the legatee, heir, or beneficiary.

SEC. 230. In lieu of the tax imposed by section 230 of the Revenue Act of 1921 there shall be levied, collected, and paid for each taxable year upon the net income of every corporation a tax of 12½ per centum of the amount of the net income in excess of the credits provided in sections 236 and 263.

(U. S. C., Title 26, Sec. 981.)

The corresponding provisions of the Revenue Act of 1926, c. 27, 44 Stat. 9, are identical except as to the rates of tax.

Revenue Act of 1928, c. 852, 45 Stat. 791, 880:

SEC. 704. TAXABILITY OF TRUSTS AS CORPORATIONS—RETROACTIVE.

(a) If a taxpayer filed a return as a trust for any taxable year prior to the taxable year 1925 such taxpayer shall be taxable as a trust for such year and not as a corporation, if such taxpayer was considered to be taxable as a trust and not as a corporation either (1) under the regulations in force at the time the return was made or at the time of the termination of its existence, or (2) under any ruling of the Commissioner or any duly authorized officer of the Bureau of Internal Revenue applicable to any of such years, and interpretative of any provision of the Revenue Act of 1918, 1921, or 1924, which had not been reversed or revoked prior to the time the return was made, or under any such ruling made after the return was filed which had not been reversed or revoked prior to the time of the termination of the taxpayer's existence.

(b) For the purpose of the Revenue Act of 1926 and prior Revenue Acts, a trust shall, at the option of the trustee exercised within one year after the enactment of this Act, be considered as a trust the income of which is taxable (whether distributed or not) to the beneficiaries, and not as an association, if such trust (1) had a single trustee, and (2) was created and operated for the sole purpose of liquidating real property as a single venture (with such powers of administration as are incidental thereto, including the acquisition, improvement, conservation, division, and sale of such property), distributing the proceeds therefrom in due course to or for the benefit of the

beneficiaries, and discharging indebtedness secured by the trust property, and (3) has not made a return for the taxable year as an association.

Treasury Regulations 65, promulgated October 6, 1924, under the Revenue Act of 1924:

ART. 1502. *Association.* — Associations and joint-stock companies include associations, common law trusts, and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the shareholders on the basis of the capital stock which each holds, or, where there is no capital stock, on the basis of the proportionate share or capital which each has or has invested in the business or property of the organization. A corporation which has ceased to exist in contemplation of law but continues its business in corporate form is an association or corporation within the meaning of section 2, but if it continues its business in the form of a trust, it becomes subject to the provisions of section 219.

ART. 1504. *Association distinguished from trust.*—Holding trusts, in which the trustees are merely holding property for the collection of the income and its distribution among the beneficiaries, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, are not associations within the meaning of the law. The trust and the beneficiaries thereof will be subject to tax as provided in articles 341–347. Operating trusts, whether or not of the Massachusetts type, in which the trustees are not restricted to the

mere collection of funds and their payments to the beneficiaries, but are associated together in much the same manner as directors in a corporation for the purpose of carrying on some business enterprise, are to be deemed associations within the meaning of the Act, regardless of the control exercised by the beneficiaries.

T. D. 3749, IV–2 Cumulative Bulletin 6, promulgated August 31, 1925, amended Article 1502 of Treasury Regulations 65 by changing the last sentence to read as follows:

> A corporation which has ceased to exist in contemplation of law but continues its business in quasi corporate form is an association or corporation within the meaning of section 2.

T. D. 3748, IV–2 Cumulative Bulletin 7, promulgated August 31, 1925, amended Article 1504 of Treasury Regulations 65 to read as follows:

> ART. 1504. *Association distinguished from trust.*—Where trustees merely hold property for the collection of the income and its distribution among the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, and the beneficiaries have no control over the trust although their consent may be required for the filling of a vacancy among the trustees or for a modification of the terms of the trust, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by section 219 and by articles 341–347. If, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists within the meaning of section 2.

> Even in the absence of any control by the beneficiaries, where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the statute.

Articles 1502 and 1504 of Treasury Regulations 69, promulgated under the Revenue Act of 1926, are the same as Articles 1502 and 1504 of Treasury Regulations 65, amended by T. D. 3749 and T. D. 3748, *supra*.

Articles 1312 and 1314 of Treasury Regulations 74, promulgated under the Revenue Act of 1928, are the same as Articles 1502 and 1504 of Treasury Regulations 69.

Article 1312 of Treasury Regulations 77, promulgated under the Revenue Act of 1932, is the same as Article 1312 of Regulations 74, but Article 1314 of Treasury Regulations 77 was changed to read as follows:

> ART. 1314. *Association distinguished from trust.*—Where trustees merely hold property for the collection of the income and its distribution among the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by sections 161–170 and by articles 861–891. Where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but have similar or greater powers than the directors

in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the Act.

Articles 801–2 and 801–3 of Treasury Regulations 86, promulgated under the Revenue Act of 1934, are as follows:

ART. 801–2. *Association.*—The term "association" is not used in the Act in any narrow or technical sense. It includes any organization, created for the transaction of designated affairs, or the attainment of some object, which, like a corporation, continues notwithstanding that its members or participants change, and the affairs of which, like corporate affairs, are conducted by a single individual, a committee, a board, or some other group, acting in a representative capacity. It is immaterial whether such organization is created by an agreement, a declaration of trust, a statute, or otherwise. It includes a voluntary association, a joint-stock association or company, a "business" trust, a "Massachusetts" trust, a "common law" trust, an "investment" trust (whether of the fixed or the management type), an interinsurance exchange operating through an attorney in fact, a partnership association, and any other type of organization (by whatever name known) which is not, within the meaning of the Act, a trust or an estate, or a partnership. If the conduct of the affairs of a corporation continues after the expiration of its charter, or the termination of its existence, it becomes an association.

ART. 801–3. *Association distinguished from trust.*—The term "trust," as used in the Act, refers to an ordinary trust, namely, one created by will or by declaration of the

trustees or the grantor, the trustees of which take title to the property for the purpose of protecting or conserving it as customarily required under the ordinary rules applied in chancery and probate courts. The beneficiaries of such a trust generally do no more than accept the benefits thereof and are not the voluntary planners or creators of the trust arrangement. Even though the beneficiaries do create such a trust, it is ordinarily done to conserve the trust property without undertaking any activity not strictly necessary to the attainment of that object.

As distinguished from the ordinary trust described in the preceding paragraph is an arrangement whereby the legal title to the property is conveyed to trustees (or a trustee) who, under a declaration or agreement of trust, hold and manage the property with a view to income or profit for the benefit of beneficiaries. Such an arrangement is designed (whether expressly or otherwise) to afford a medium whereby an income or profit-seeking activity may be carried on through a substitute for an organization such as a voluntary association or a joint-stock company or a corporation, thus obtaining the advantages of those forms of organization without their disadvantages.

If a trust is an undertaking or arrangement conducted for income or profit, the capital or property of the trust being supplied by the beneficiaries, and if the trustees or other designated persons are, in effect, the managers of the undertaking or arrangement, whether the beneficiaries do or do not appoint or control them, the beneficiaries are to be treated as voluntarily joining or cooperating with each other in the trust, just as do members of an association, and the

undertaking or arrangement is deemed to be an association classified by the Act as a corporation.

By means of such a trust the disadvantages of an ordinary partnership are avoided, and the trust form affords the advantages of unity of management and continuity of existence which are characteristic of both associations and corporations. This trust form also affords the advantages of capacity, as a unit, to acquire, hold, and dispose of property and the ability to sue and be sued by strangers or members, which are characteristic of a corporation; and also frequently affords the limitation of liability and other advantages characteristic of a corporation. These advantages which the trust form provides are frequently referred to as resemblance to the general form, mode of procedure, or effectiveness in action, of an association or a corporation, or as "quasi-corporate form." The effectiveness in action in the case of a trust or of a corporation does not depend upon technical arrangements or devices such as the appointment or election of a president, secretary, treasurer, or other "officer," the use of a "seal," the issuance of certificates to the beneficiaries, the holding of meetings by managers or beneficiaries, the use of a "charter" or "by-laws," the existence of "control" by the beneficiaries over the affairs of the organization, or upon other minor elements. They serve to emphasize the fact that an organization possessing them should be treated as a corporation, but they are not essential to such classification, for the fundamental benefits enjoyed by a corporation, as outlined above, are attained, in the case of a trust, by the use of the trust form *itself*. The Act

disregards the technical distinction between a trust agreement (or declaration) and ordinary articles of association or a corporate charter, and all other differences in detail. It treats such a trust according to its essential nature, namely, as an association. This is true whether the beneficiaries form the trust or, by purchase or otherwise, acquire an interest in an existing trust.

The mere size or amount of capital invested in the trust is of no importance. Sometimes the activity of the trust is a small venture or enterprise, such as the division and sale of a parcel of land, the erection of a building, or the care and rental of an office building or apartment house; sometimes the activity is a trade or business on a much larger scale. The distinction is that between the activity or purpose for which an ordinary strict trust of the traditional type would be created, and the activity or purpose for which a corporation for profit might have been formed.

Treasury Regulations 62, promulgated under the Revenue Act of 1921:

ART. 1502. *Association.*—Associations and joint-stock companies include associations, common law trusts, and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the members or shareholders on the basis of the capital stock which each holds or, where there is no capital stock, on the basis of the proportionate share or capital which each has or has invested in the business or property of the

organization. A corporation which has ceased to exist in contemplation of law but continues its business in corporate form is an association or corporation within the meaning of section 2, but if it continues its business in the form of a trust, it becomes subject to the provisions of section 219.

ART. 1504. *Association distinguished from trust.*—Where trustees hold real estate subject to a lease and collect the rents, doing no business other than distributing the income less taxes and similar expenses to the holders of their receipt certificates, who have no control except the right of filling a vacancy among the trustees and of consenting to a modification of the terms of the trust, no association exists and the cestuis que trust are liable to tax as beneficiaries of a trust the income of which is to be distributed periodically, whether or not at regular intervals. But in such a trust if the trustees pursuant to the terms thereof have the right to hold the income for future distribution, the net income is taxed to the trustees instead of to the beneficiaries. See section 219 of the statute and articles 341–348. If, however, the cestuis que trust have a voice in the conduct of the business of the trust, whether through the right periodically to elect trustees or otherwise, the trust is an association within the meaning of the statute.

APPENDIX "B"

DECISIONS OF THE CIRCUIT COURT OF APPEALS FOR THE FIRST CIRCUIT

In the early case of *White* v. *Hornblower,* 27 F. (2d) 777, a stamp tax case, and in *United States* v. *Neal,* 28 F. (2d) 1022, reversing *per curiam* the decision of the District Court, 26 F. (2d) 708, certiorari denied, 278 U. S. 659, the Circuit Court of Appeals for the First Circuit apparently accepted the business test as conclusive. Again, in *Gardiner* v. *United States,* 49 F. (2d) 992, the court considered that the test was whether the trust was transacting business for profit. See also *Lansdowne Realty Trust* v. *Commissioner,* 50 F. (2d) 56; *Dunbar* v. *Commissioner,* 65 F. (2d) 447.

In some of its more recent decisions, however, it has rejected that test as decisive and has relied in part on whether the forms of a corporation were followed in the conduct of business. For instance, in *Commissioner* v. *Kelley,* 74 F. (2d) 71, the court held that a trust which was organized by members of a partnership conducting a glue business was not an association, though there could be no question but what the trust was transacting business just as the partnership had. In that case the court said that in some cases courts had emphasized form and in others whether the trust was carrying on a business, but that there was no law prohibiting the trustees from doing business and that there were two tests, namely, whether the association was

doing business and whether it followed the forms of a corporation.

To the same effect is *Coleman-Gilbert Associates* v. *Commissioner,* 76 F. (2d) 191, now pending in this Court on petition for certiorari, Nos. 78 & 79, October Term, 1935, in which the court said (p. 194):

> We think, however, it is generally agreed that, in order for a trust to be taxed as a corporation, the trustees must not only be carrying on a business enterprise for profit, but must be doing it in much the same manner and form as directors of a corporation.

DECISIONS OF THE CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT

The court applied the business test in *Allen* v. *Commissioner,* 49 F. (2d) 716, certiorari denied, 284 U. S. 655, concluding that the particular trust was merely engaged in holding securities for a limited time and purpose and was consequently not an association.

In *Ittleson* v. *Anderson,* 67 F. (2d) 323, a capital stock case, the court rejected the test of a quasi-corporate form and held that the trustees were engaged in sufficient activities for the trust to be taxed as an association.

See also *Investment Trust of Mutual Investment Co.* v. *Commissioner,* 27 B. T. A. 1322, affirmed *per curiam,* 71 F. (2d) 1009.

DECISIONS OF THE CIRCUIT COURT OF APPEALS FOR THE THIRD CIRCUIT

In *Little Four Oil & Gas Co.* v. *Lewellyn,* 35 F. (2d) 149, certiorari denied, 280 U. S. 613, the court

stated that the theory that the distinction between trusts is based on the powers exercised by shareholders was no longer seriously regarded and that the test was whether the shareholders or trustees or both combined carried on a business for profit. It thus clearly emphasized the business test, although as a matter of fact some of the forms of a corporation were followed in the transaction of business by the trust.

That such was the conclusion of the court is settled by its decision in *Smith* v. *Commissioner,* 69 F. (2) 911, certiorari denied, 293 U. S. 561:

See also *Harmer Coal Co.* v. *Heiner,* 34 F. (2d) 725 (a capital stock tax case), certiorari denied, 280 U. S. 610.

DECISIONS OF THE CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

In *Blair* v. *Wilson Syndicate Trust,* 39 F. (2d) 43, the court held that the trust was a pure trust and was not an association, and in doing so apparently distinguished between an ancestral trust and a voluntary trust. Nothing very clear was said in that case on the subject of the necessity of corporate form.

In *Lucas* v. *Extension Oil Co.,* 47 F. (2d) 65, the court emphasized the lack of resemblances to a corporation and concluded that the trust was neither in business nor had such corporate structure as brought it within the definition of an association.

In *Commissioner* v. *Guitar Trust Estate,* 72 F. (2d) 544, a husband and wife created a trust for the benefit of their children and conveyed most of their property, including a variety of business

enterprises, to it. In that case the court emphasized both the lack of control by the certificate holders and the lack of resemblances to a corporation, and said that the fact that the duties of the trustee included carrying on a going business was not material. Cf. *Gray* v. *Hopkins,* 68 F. (2d) 561, certiorari denied, 292 U. S. 643, which, however, turns largely upon the application of Section 704 (a) of the Revenue Act of 1928. See also *Commissioner* v. *Commercial Trust Co.,* 56 F. (2d) 1080, reversing *per curiam* 21 B. T. A. 732.

DECISIONS OF THE CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT

The decisions of this circuit do not appear to be entirely consistent, although in general the court has considered that it is necessary for some corporate attributes to be present.

In *Sears, Roebuck & Co. Employees' Savings, etc.,* v. *Commissioner,* 45 F (2d) 506, it was held that an employee's savings and profit sharing fund was taxable as an association, although there were no certificates of beneficial interest and a number of other attributes of a corporation were lacking.

In *Tyson* v. *Commissioner,* 54 F. (2d) 29, the court apparently relied on the absence of corporate forms and on the absence of beneficiary control, as well as upon the lack of business activity.

In the later case of *Tyson* v. *Commissioner,* 68 F. (2d) 584, certiorari denied, 292 U. S. 657, involving a different real estate trust, the court found that the trustee was engaged in enough activities to amount to carrying on a business, but it also relied upon the existence of certain corpo-

rate attributes including transferable certificates and the resemblance of the trustees to a board of directors. See also *Commissioner* v. *Duckwitz*, 68 F. (2d) 629, and *Commissioner* v. *McCormick*, 68 F. (2d) 653.

In *Commissioner* v. *Morriss R. Co. Trust No. 2*, 68 F. (2d) 648, the court held that the activities engaged in were not sufficient to constitute an association and apparently regarded that as the more important test, although it mentioned the lack of corporate organization.

In *Reinecke* v. *Kaempfer*, 72 F. (2d) 469, certiorari denied, 294 U. S. 708 (involving a capital stock tax), the court again considered it necessary that there should be resemblances to a corporation but emphasized resemblances in substance rather than in form.

In *Swanson* v. *Commissioner*, 76 F. (2d) 651, which is now pending before this Court on petition for a writ of certiorari, No. 108, October Term, 1935, two individuals owning an apartment building transferred the property to three trustees to manage. One half of the original shares of beneficial interest went to each grantor, but they were subsequently transferred to their wives. The record showed that the trustees did not have formal meetings and left everything to one trustee, who was a partner in another business. The court apparently emphasized the business test and to the extent that it paid any attention to corporate structure seems to have emphasized resemblances in substance rather than form.

The decisions of the Circuit Court of Appeals for the Ninth Circuit are more consistent, generally speaking, than those of any other circuit with reference to this question.

In the case of *Trust No. 5833, Security-First Nat. Bank* v. *Welch,* 54 F. (2d) 323, certiorari denied, 286 U. S. 544, the court stated that the real test was whether the shareholders or trustees or both combined carried on business for profit and that it was immaterial whether the shares of interests in the project were evidenced by certificates of stock.

To the same effect is *Commissioner* v. *Atherton,* 50 F. (2d) 740, where it was held that the trust was not an association because it was organized by a transit company solely for the purpose of liquidating its real estate holdings and that it did no business except to collect rent and pay taxes on the parcels involved until the land was sold.

In *Sloan* v. *Commissioner,* 63 F. (2d) 666, the business test was again emphasized and it was held that the trust was an association because it had originally been organized to lease, mortgage and sell lands in a subdivision, even though all of the lands had been sold and during the taxable year involved the trustees' activities were limited to the collection and distribution of installment payments. See also *Willis* v. *Commissioner,* 58 F. (2d) 121.

Again, in *Twin Bell Oil Syndicate* v. *Helvering,* 70 F. (2d) 402, reversed on other grounds, 293 U. S. 312, the court said (p. 407):

There is ample additional authority for the proposition that the "business" test is now paramount.

The decision in the *Morrissey* case, therefore, is in accord with the general trend of decisions in the Ninth Circuit. In one case, however, that of *Commissioner* v. *Combs,* 76 F. (2d) 682, which is now pending before this Court on petition for a writ of certiorari, No. 238, October Term, 1935, the court departed from the view that the business test was paramount and held that the trust must also use the corporate method of transacting business in order to be taxed as an association. This decision is clearly contrary to the court's previous decisions, none of which it expressly overruled.

DECISIONS OF THE CIRCUIT COURT OF APPEALS FOR THE TENTH CIRCUIT

In *Commissioner* v. *Brouillard,* 70 F. (2d) 154, certiorari denied *sub nom., Helvering* v. *Pryor & Lockhart Development Co.,* 293 U. S. 574,* the court defined an association as a body of persons united without charter but employing the methods, modes and procedural forms of a corporation, and suggested that the resemblances to a corporation should be balanced. The court definitely rejected the claim that the doing of business was sufficient.

---

* One of the syndicates before the court in this case was also before the court in *Commissioner* v. *Duckwitz, supra.* The same syndicate was before the Circuit Court of Appeals for the Eighth Circuit in *Burnet* v. *Burns,* 63 F. (2d) 313, where the court held that it was a joint venture. We have not discussed the decisions of that Circuit as that case is the only one on the subject and it does not lay down a clear test.

The Board's decisions cannot be reconciled. In the following cases it apparently has emphasized the test of "doing business" without regard to quasi-corporate form. *Woodrow Lee Trust* v. *Commissioner*, 14 B. T. A. 1420; *Dauphin Deposit Trust Co.* v. *Commissioner*, 21 B. T. A. 1214; *Carlson* v. *Commissioner*, 27 B. T. A. 93, now pending in the Circuit Court of Appeals for the Ninth Circuit; *Tulsa Mortgage Investment Co.* v. *Commissioner*, 21 B. T. A. 735; *Dutton* v. *Commissioner*, 18 B. T. A. 1151.

In the following cases the Board accepted the necessity of there being a resemblance to a corporation in mode of procedure. *Sturgeon* v. *Commissioner*, 25 B. T. A. 368; *Cyclops Iron Works* v. *Commissioner*, 25 B. T. A. 603; *Jackson-Wermich Trust* v. *Commissioner*, 24 B. T. A. 150; *Dolese & Shepherd Co.* v. *Commissioner*, 30 B. T. A. 1171,

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IN THE

Supreme Court of the United States

October Term, 1935

No. 17

T. A. MORRISSEY and JAMES M. O'BRIEN, Trustees of an Express Trust, known as Western Avenue Golf Club, *Petitioners,*

against

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

On Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit

MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE,* AND BRIEF

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MOTION FOR LEAVE TO FILE BRIEF AS *AMICUS CURIAE*

May it please the Court:

The undersigned, Claude A. Hope, respectfully moves the Court for leave to file the accompanying brief, as *amicus curiae*, and in support of this motion, shows unto the Court as follows:

The essential question to be determined by this Court is the construction of the word "association" when used in a tax statute.

The undersigned is not employed as counsel in the above-entitled case, but is counsel for the trustees of several investment trusts which the Bureau of Internal Revenue has heretofore held to be strict trusts, and not associations. The decision in this case as to the correct meaning of the word "association" will largely determine whether these trusts will continue to be held taxable as strict trusts and not as associations. Many thousands of investors are beneficiaries of these trusts which represent an investment of many millions of dollars.

The purpose of this brief is to present to this Court the view that the word "association" when used in a statute imposing taxes or other liabilities is uniformly held to include only organizations which do business for profit under the usual forms and procedure of corporations.

The attorneys for the respondent and the attorneys for petitioners have consented in writing to the filing of this brief by the undersigned.

The undersigned therefore requests that this Court permit him to file the following brief as *amicus curiae* in the above-entitled matter.

CLAUDE A. HOPE,
20 Exchange Place,
New York, New York.
Amicus Curiae.

JOHN ROSS DELAFIELD,
Of Counsel.

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COMMISSIONER OF INTERNAL REVENUE,
Respondent.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit

BRIEF OF *AMICUS CURIAE*

Preliminary Statement

The above entitled case presents to the Court the necessity of determining whether the organization involved, the Western Avenue Golf Club, is an "association" or a "trust" under the Revenue Acts of 1924 and 1926 and the regulations issued thereunder. This general question is not new. It has been before the lower Courts and the Bureau of Internal Revenue a great many times and in a great many forms.

The Revenue Acts have always provided that "associations" should be treated as corporations. No subsequent Act has changed the original wording of the Revenue Act of 1918 that "The term 'corporation' includes associations, joint stock companies, and insurance companies" (Sec. 1, c. 18, 40 Stat. 1057). The sentence as quoted appears unchanged in the current Revenue Act.

On August 31, 1925, the Treasury Department adopted a regulation, discussed elsewhere in this brief, establishing certain tests under which some organizations, admittedly common law trusts, were to be treated under the Revenue Act as "associations" and, therefore, were to be subjected to taxation as corporations. The regulation followed closely the prineiples laid down in a number of cases decided prior to its adoption, including the decision of this Court in *Hecht* v. *Malley*, 265 U. S. 144. A great many specific rulings were issued under it by the Commissioners of Internal Revenue. A large number of organizations were formed relying upon the regulation and the announced rulings as establishing the law applicable to the question,—at least until the Congress saw fit, by appropriate amendment of the law, to change it.

During recent months there has been a distinct tendency on the part of the Bureau to stray from these established tests. See, for example, Arts. 801-2 and 801-3 of Treasury Department Regulations 86 (the regulations under the Revenue Act of 1934) which are set forth in the Appendix hereto. Notwithstanding the fact that there has been no change in the statute, these regulations entirely disregard the fundamental test established by the Courts that a trust, in order to be taxable as an association, must be engaged in business for profit under the usual forms and procedure of corporations.

A great many trusts which for many years, in accordance with specific rulings previously obtained, have filed tax returns under the appropriate Revenue Acts as strict trusts and not as associations, are faced with the distinct possibility of a reversal of those rulings. It is believed that the decision in the case at bar will have a substantial if not controlling effect upon the determination of the ultimate taxable status of such organizations. The case before the Court, therefore, will undoubtedly have consequences of far greater importance than is indicated by the facts presented and the amount involved. Many thousands of persons and many millions of dollars in property will be affected. In the field of non-discretionary investment trusts alone, which trusts are formed under common law trust indentures, there is upwards of $100,000,000 involved affecting perhaps 100,000 or more persons. This brief is filed on behalf of trustees acting for several such trusts having approximately $54,360,000 in property and approximately 63,500 beneficiaries.

The trustees and beneficiaries of these trusts, who are not parties to the litigation before the Court, are primarily interested, not in the outcome of the instant case, but in the rules or tests which this Court may lay down in determining whether the trust before it is, for taxation purposes, a strict trust or an association, and particularly are they interested in the maintenance and continuation of the well established rule that the word "association" when used in a taxing statute includes only organizations which do business for profit under the usual forms and procedure of corporations.

THE ARGUMENT

I

The word "association" when used in a statute imposing taxes or other liabilities is uniformly held to include only organizations which do business for profit under the usual forms and procedure of corporations.

In re The St. James's Club, 13 English Law & Eq. 589 (1852), was an appeal from an order of the Vice-Chancellor whereby he ordered the above association to be dissolved and referred it to the Master to wind up the affairs of the club under the provisions of the Winding-up Acts, 11 & 12 Vict, c. 45 as amended by 12 & 13 Vict. c. 108. The appellant urged that the Winding-up Acts did not apply as the association was not established for profit. 12 & 13 Vict. c. 108 amended 11 & 12 Vict. c. 45 and provided

> "that notwithstanding anything in the said act contained importing a more limited application thereof, the same shall apply to all partnerships, associations, and companies * * * "

The Lord Chancellor (Lord St. Leonards) held that the club was not an association within the meaning of the Act, and said:

> "Now, although the word 'association' is here used, and though an 'association' may include bodies of persons who are neither partners nor members of a company, properly so called, yet it would be difficult to convince me that the word 'association,' occurring as it does between those two words, 'partnership' and 'company,' is to be treated generally—that is, to mean every association, without reference to the particular bodies with which the term is so closely associated. * * * An 'association' it is, but

> not an 'association' within the meaning of the statute, considering between what words we find the word introduced in the statute. When I look, therefore, at this latter statute, I find that every provision in it is inconsistent with the notion that the legislature intended to include clubs in the word 'association.' If it did so intend, how is it that we do not find the word 'club' in the act? Clubs are very well known to exist, and it is impossible to suppose that the word would not have found its way into the act, had the legislature intended to include them. And I think that the judges are bound not to extend unnecessarily the meaning of words thus ambiguous to institutions which are well known to exist to a very great extent, and might have been introduced by a word" (p. 594).

In *Hecht* v. *Malley*, 265 U. S. 144 (1924), this Court said at page 157:

> "We think that the word 'association,' as used in the Act, clearly includes 'Massachusetts Trusts' such as those herein involved, having quasi-corporate organizations under which they are engaged *in carrying on business enterprises.* What other form of 'associations,' if any, it includes, we need not, and do not, determine." (Italics ours.)

The Circuit Courts of Appeals for the First, Second, Third, Fifth, Seventh, and Ninth Circuits have held that a trust must be engaged in doing business for profit in order to constitute an association within the meaning of the Revenue Acts.

First Circuit

In *Lansdowne Realty Trust* v. *Commissioner*, 50 Fed. (2d) 56 (C. C. A., 1st Cir), the Court said at page 58:

> "We are also of the opinion that the trust was

not an association and taxable as a corporation on the ground that it was doing business as such.

* * * * *

By the terms of the lease the lessees were to keep the premises in repair, pay the insurance, and be responsible for all damages connected with the building. It is perfectly apparent that they were not doing business in any sense, during the years 1923 and 1924, and we are of the opinion that, during the years 1925 and 1926, *they were not conducting business* after the mode and manner of a corporation, but were doing nothing more than trustees ordinarily would be called upon to perform in the management of trust property." (Italics ours.)

In *Commissioner of Internal Revenue* v. *Kelley*, 74 Fed. (2d) 71 (C. C. A., 1st Cir.), the Court said at page 75:

"To constitute a trust an association, and taxable as a corporation, there must be a body of persons associated together who are (1) actually carrying on business for profit, and (2) under the usual forms and procedure of corporations. Both conditions must be present."

In *Coleman-Gilbert Associates* v. *Commissioner*, 76 Fed. (2d) 191 (C. C. A., 1st Cir.), the Court said at page 194:

"We think, however, it is generally agreed that, in order for a trust to be taxed as a corporation, the trustees must not only be carrying on a business enterprise for profit, but must be doing it in much the same manner and form as directors of a corporation."

Second Circuit

In *Allen* v. *Commissioner*, 49 Fed. (2d) 716 (C. C. A., 2nd Cir.), certiorari denied 284 U. S. 655, the Court said at page 717:

"This was not a trust like those before the Court in *Hecht* v. *Malley*, 265 U. S. 144, 44 S. Ct. 462, 68 L. Ed. 949, where the trustee *was conducting a business.* The only purpose was to hold the assets as security for a season, and then to distribute them." (Italics ours.)

Third Circuit

In *Little Four Oil & Gas Co.* v. *Lewellyn*, 35 Fed. (2d) 149 (C. C. A., 3rd Cir.), certiorari denied 280 U. S. 613, the Court said at page 150:

"The theory that the distinction between trusts of these classes and their consequent liability for taxes is based on the powers exercised by the shareholders—great or little—is no longer seriously regarded. *The real test is whether the shareholders or trustees, or both combined, carry on business for profit*, and, if they do, they constitute a business trust—in legal effect an association or a joint-stock company—with liability for taxes." (Italics ours.)

In *Smith* v. *Commissioner*, 69 Fed. (2d) 911 (C. C. A., 3rd Cir.), certiorari denied 293 U. S. 561, the court said at page 912:

"The test laid down by this court in *Little Four Oil & Gas Co.* v. *Lewellyn* (C. C. A.) 35 F. (2d) 149, is that, *if the trust is a business concern*, and if the shareholders or trustees, or both combined, *are operating it in active business for profit*, the trust is in effect an association taxable as a 'corporation.'" (Italics ours.)

Fifth Circuit

In *Lucas* v. *Extension Oil Co.*, 47 Fed. (2d) 65 (C. C. A., 5th Cir.) the court said at page 67:

"Believing that it would be a wresting of judg-

ment to hold under the facts of this case that respondent was within the statute invoked *doing a corporate business,* and subject to be taxed as a corporation, the petition for review of the judgment of the Board of Tax Appeals is denied, and the judgment is affirmed." (Italics ours.)

Seventh Circuit

In *Reinecke* v. *Kaempfer,* 72 Fed. (2d) 469, (C. C. A., 7th Cir.) the court said at page 470:

> "It is plain that from its inception the business was carried on for profit. * * *
>
> We are satisfied that the similitude referred to is not in those essentials which distinctly stamp the entity as a corporation, but rather in the business carried on and the manner of its transaction. This entity carried on its business in substantially the same way that a corporation would have carried it on. It regularly bought and sold merchandise for the purpose of realizing profit thereon; * * *"

Ninth Circuit

In *Trust No. 5833, Security-First Nat'l. Bank* v. *Welch,* 54 Fed. (2d) 323 (C. C. A., 9th Cir.) certiorari denied 286 U. S. 544, the court said at page 327:

> "If we accept, as we think we should, the interpretation placed upon the word 'association' by the Commissioner of Internal Revenue, inferentially approved and adopted by Congress in subsequent legislation, based upon the decision of the Supreme Court in *Hecht* v. *Malley, supra,* it follows that there are two criteria for determining whether or not an organization or combination of individuals is taxable as an association. The first test found in article 1312 is *the business test;* that is to say, the test

> as to whether or not the organization formed '*to do business* in an organized capacity' and for the distribution *of the profits* among the shareholders in proportion to the investment or shares." (Italics ours).

In *Willis* v. *Commissioner*, 58 Fed. (2d) 121 (C. C. A., 9th Cir.), the court said at page 122:

> "Simply stated, the question is, did the trustees manage and operate the property in their charge *as a business*, with the purpose to *accumulate a profit* by the use of it, or was their sole purpose, intended and pursued, to dispose of it as rapidly as possible, market conditions considered, and divide the proceeds among the beneficiaries? As a liquidating trust purely, the income would not be taxable; as a business venture, the income would be taxable." (Italics ours.)

In *Sloan* v. *Commissioner*, 63 Fed. (2d) 666 (C. C. A., 9th Cir.) the court said at page 669:

> "We think that petitioners are an association within the meaning of the law and regulations of the Treasury Department, and that they were engaged in business for profit during the taxable years in question."

In *Twin Bell Oil Syndicate* v. *Helvering*, 70 Fed. (2d) 402 (C. C. A., 9th Cir.); which was reversed on another issue in 293 U. S. 312, the court said at page 407:

> "There is ample additional authority for the proposition that the 'business' test is now paramount."

Tenth Circuit

At first glance it might appear that the Circuit Court of Appeals for the Tenth Circuit has rejected the business

test in its decision in *Commissioner* v. *Pryor & Lockhart Development Co.*, 70 Fed. (2d) 154, certiorari denied 293 U. S. 574, because its decision contains the following statement:

> "The fact that a group of persons associate themselves together for the purpose of engaging in business for profit does not necessarily mean that they must be taxed as an association. That is not the decisive consideration."

In that case certain persons interested in oil leases conveyed property to trustees to sell interests therein and develop leases. The trustees decided what wells should be drilled and sold the oil. No officers were elected and, except in one instance, no meetings of the beneficiaries were held. The beneficiaries exercised no control over the trustees. It was held that the trusts were not associations under the Revenue Acts of 1918, 1924, 1926 and 1928. It is therefore to be noted that the Circuit Court of Appeals for the Tenth Circuit did not reject the business test as a necessary test, but merely said that the business test was not the only test. In the case cited, the trust was plainly engaged in business, yet it was held not taxable as an association because its business was not conducted after the method and form of a corporation.

No case involving the question under consideration has been found in the Fourth, Sixth or Eighth Circuits, either in the Circuit Courts of Appeals or in the District Courts.

It is thus seen that there is no conflict between the various Circuit Courts of Appeals as to the necessity that a trust be engaged in business for profit in order to constitute an association, and that this test is one of the tests that are invariably applied.

The decisions of the Board of Tax Appeals are to the same effect.

In *Sturgeon & Hubbard* v. *Commissioner*, 25 B. T. A. 368, the Board said:

> "This Board has held that the significant tests to be applied in determining whether an alleged trust is a trust or an association taxable as a corporation, are whether (1) the beneficiaries of the alleged trust have voluntarily associated themselves together in the general form and mode of procedure of a corporation, and (2) are organized to, and in fact are, engaged in the active conduct of a business for profit, or (3) whether the trustees are merely holding the property and collecting the income therefrom and distributing to those beneficially interested."

In *Franklin Title & Trust Co.* v. *Commissioner*, 32 B. T. A. 266 (promulgated March 28, 1935), the Board said:

> "There is a more important circumstance which alone is fatal to the contention of the trust company—this trust was not organized for the purpose of carrying on a business and, during the taxable years, it did not carry on a business, as distinguished from the normal activities of a mere fiduciary. See, for importance of 'business' test, *Twin Bell Oil Syndicate* v. *Helvering*, 70 Fed. (2d) 402, affirming on this point, 26 B. T. A. 172; *Tyson* v. *Commissioner*, 68 Fed. (2d) 584; certiorari denied, 292 U. S. 657; *Montovia Oil Co.*, 28 B. T. A. 335."

A double tax upon the income of a trust, *viz.*, a tax, first, on the income of the trust as an entity, and a further tax upon the distributive shares of the beneficiaries, should, if applied, be imposed in clear and unmistakable language in the acts of Congress, and should not have as its

basis some mere resemblance in one way or another to a corporation. As Lord St. Leonards said *In re The St. James's Club, supra,* judges are bound not to extend unnecessarily the meaning of words as ambiguous as "association" to institutions which are well known to exist to a very great extent when such institutions could have been readily covered by appropriate language. And it is well established in this court that if there is doubt, the doubt should be resolved in favor of the taxpayer (*Crocker* v. *Malley,* 249 U. S. 223, at page 233; *Hecht* v. *Malley,* 265 U. S. 144, at page 160).

And yet, if in disposing of the case before it, this Court does not include in whatever tests it lays down, the requirement, among others, that business must be carried on for profit by a trust in order for it to be taxed as an association, the effect will be to throw many organizations not specifically mentioned in the Acts, though well known to Congress to exist, into classification as associations.

II

By re-enacting in the Revenue Acts of 1926, 1928, 1932 and 1934 the provisions of Sec. 2 (a) (2) of the Revenue Act of 1924 Congress has ratified and adopted the construction of the Treasury Department of the meaning of the word "association" as contained in Art. 1504 of Treasury Department Regulations 65 as amended Aug. 31, 1925.

Sec. 2 (a) (2) of the Revenue Act of 1924 (c. 234, 43 Stat. 253) provides:

> "The term 'corporation' includes associations, joint stock companies, and insurance companies."

The same provision is contained in the Revenue Acts of 1926, 1928, 1932 and 1934. (Sec. 2, Revenue Act of 1926 (c. 27, 44 Stat. 9); Sec. 701, Revenue Act of 1928 (c. 852, 45 Stat. 791); Sec. 1111, Revenue Act of 1932 (c. 209, 47 Stat. 169); Sec. 801, Revenue Act of 1934 (c. 277, 48 Stat. 680). None of these statutes gave any definition of an association.

The regulations of the Treasury Department having to do with the distinction between a trust and an association have, from August 31st, 1925, down to the promulgation of the regulations under the Revenue Act of 1934, been based upon the decision in *Hecht* v. *Malley*, 265 U. S. 144. Art. 1504 of Treasury Regulations 65 as amended by T. D. 3748 (C. B. IV-2, page 7) on August 31st, 1925 (the regulations under the Revenue Act of 1924), is typical and is as follows:

> "Art. 1504. Association Distinguished from Trust. Where trustees merely hold property for the collection of the income and its distribution among

> the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, and the beneficiaries have no control over the trust although their consent may be required for the filling of a vacancy among the trustees or for a modification of the terms of the trust, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by Section 219 and by Articles 341-347. If, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists within the meaning of Section 2. Even in the absence of any control by the beneficiaries, where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the statute."

Since the promulgation of these regulations, Congress has re-enacted in the Revenue Acts of 1926, 1928, 1932 and 1934 the same statutory provision which was construed by the Treasury Department in the above quoted regulation. This is persuasive evidence of legislative approval of the regulation. There are also many cases which hold that such re-enactment confirmed and carried forward the policy evidenced by the earlier enactment as interpreted in the regulations promulgated under it.

In *Brewster* v. *Gage*, 280 U. S. 327, the Court said:

> "The substantial re-enactment in later Acts of the provision theretofore construed by the Department is persuasive evidence of legislative approval of the regulation."

To the same effect are *Burnet* v. *Thompson Oil & G. Co.*, 283 U. S. 301, and *Helvering* v. *Bliss*, 293 U. S. 144.

Conclusion

It therefore appears that the distinction made by Art. 1504 of Reg. 65 between a trust and an association, based upon the doing of business, is a distinction in accordance with the decisions of the courts as heretofore pointed out, and has been approved by Congress in its successive re-enactments of the provisions of the Revenue Act of 1924. Until such time as Congress shall change the statute so as specifically to provide for the taxation as corporations of common law trusts which are not engaged in doing business for profit, it is submitted that the test of doing business for profit as one of the necessary indicia of an association must continue to prevail.

Respectfully,

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APPENDIX

Regulations 86, promulgated under the Revenue Act of 1934:

REG. 86, ART. 801-2. Association.—The term "association" is not used in the Act in any narrow or technical sense. It includes any organization, created for the transaction of designated affairs, or the attainment of some object, which, like a corporation, continues notwithstanding that its members or participants change, and the affairs of which, like corporate affairs, are conducted by a single individual, a committee, a board, or some other group, acting in a representative capacity. It is immaterial whether such organization is created by an agreement, a declaration of trust, a statute, or otherwise. It includes a voluntary association, a joint-stock association or company, a "business" trust, a "Massachusetts" trust, a "common law" trust, an "investment" trust (whether of the fixed or the management type), an interinsurance exchange operating through an attorney in fact, a partnership association, and any other type of organization (by whatever name known) which is not, within the meaning of the Act, a trust or an estate, or a partnership. If the conduct of the affairs of a corporation continues after the expiration of its charter, or the termination of its existence, it becomes an association.

REG. 86, ART. 801-3. Association distinguished from trust.—The term "trust" as used in the Act, refers to an ordinary trust, namely, one created by will or by declaration of the trustees or the grantor, the trustees of which take title to the property for the purpose of protecting or conserving it as customarily required under the ordinary rules applied in chancery and probate courts. The beneficiaries of such a trust generally do no more than accept the benefits thereof and are not the voluntary planners nor creators of the

trust arrangement. Even though the beneficiaries do create such a trust, it is ordinarily done to conserve the trust property without undertaking any activity not strictly necessary to the attainment of that object.

As distinguished from the ordinary trust described in the preceding paragraph is an arrangement whereby the legal title to the property is conveyed to trustees (or a trustee) who, under a declaration or agreement of trust, hold and manage the property with a view to income or profit for the benefit of beneficiaries. Such an arrangement is designed (whether expressly or otherwise) to afford a medium whereby an income or profit-seeking activity may be carried on through a substitute for an organization such as a voluntary association or a joint-stock company or a corporation, thus obtaining the advantages of those forms of organization without their disadvantages.

If a trust is an undertaking or arrangement conducted for income or profit, the capital or property of the trust being supplied by the beneficiaries, and if the trustees or other designated persons are, in effect, the managers of the undertaking or arrangement, whether the beneficiaries do or do not appoint or control them, the beneficiaries are to be treated as voluntarily joining or cooperating with each other in the trust, just as do members of an association, and the undertaking or arrangement is deemed to be an association classified by the Act as a corporation.

By means of such a trust the disadvantages of an ordinary partnership are avoided, and the trust form affords the advantages of unity of management and continuity of existence which are characteristic of both associations and corporations. This trust form also affords the advantages of capacity, as a unit, to acquire, hold, and dispose of property and the ability to sue and be sued by strangers or members, which are characteristic of a corporation; and also frequently affords the limitation of liability and other advan-

tages characteristic of a corporation. These advantages which the trust form provides are frequently referred to as resemblance to the general form, mode of procedure, or effectiveness in action, of an association or a corporation, or as "quasi corporate form." The effectiveness in action in the case of a trust or of a corporation does not depend upon technical arrangements or devices such as the appointment or election of a president, secretary, treasurer, or other "officer," the use of a "seal," the issuance of certificates to the beneficiaries, the holding of meetings by managers or beneficiaries, the use of a "charter" or "by-laws," the existence of "control" by the beneficiaries over the affairs of the organization, or upon other minor elements. They serve to emphasize the fact that an organization possessing them should be treated as a corporation, but they are not essential to such classification, for the fundamental benefits enjoyed by a corporation, as outlined above, are attained, in the case of a trust, by the use of the trust form *itself*. The Act disregards the technical distinction between a trust agreement (or declaration) and ordinary articles of association or a corporate charter, and all other differences of detail. It treats such a trust according to its essential nature, namely, as an association. This is true whether the beneficiaries form the trust or, by purchase or otherwise, acquire an interest in an existing trust.

The mere size or amount of capital invested in the trust is of no importance. Sometimes the activity of the trust is a small venture or enterprise, such as the division and sale of a parcel of land, the erection of a building, or the care and rental of an office building or apartment house; sometimes the activity is a trade or business on a much larger scale. The distinction is that between the activity or purpose for which an ordinary strict trust of the traditional type would be created, and the activity or purpose for which a corporation for profit might have been formed.

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SUPREME COURT OF THE UNITED STATES.

No. 17.—October Term, 1935.

T. A. Morrissey and James M. O'Brien, Trustees of an Express Trust known as Western Avenue Golf Club, Petitioners,
vs.
Commissioner of Internal Revenue.

On Writ of Certiorari to the United States Circuit Court of Appeals for the Ninth Circuit.

[December 16, 1935.]

Mr. Chief Justice Hughes delivered the opinion of the Court.

Petitioners, the trustees of an express trust, contest income taxes for the years 1924 to 1926, inclusive, upon the ground that the trust has been illegally treated as an "association". The Circuit Court of Appeals affirmed the decision of the Board of Tax Appeals which sustained the ruling of the Commissioner of Internal Revenue. 74 F. (2d) 803. We granted certiorari because of a conflict of decisions as to the distinction between an "association" and a "pure trust", the decisions being described in one of the cases as "seemingly in a hopeless state of confusion". *Helvering* v. *Coleman-Gilbert Associates*, 76 F. (2d) 191, 193.[1]

The facts were stipulated. In the year 1921 petitioners made a declaration of trust of real estate in Los Angeles. They were to be designated in "their collective capacity" as "Western Avenue Golf Club". The trustees were authorized to add to their number and to choose their successors; to purchase, encumber, sell, lease and operate the "described or other lands"; to construct and operate golf courses, club houses, etc.; to receive the rents, profits and income; to make loans and investments; to make regulations; and generally to manage the trust estate as if the trustees were its absolute owners. The trustees were declared to be without power to bind the beneficiaries personally by "any act, neglect or default", and the beneficiaries and all persons dealing with the trustees were required to look for payment or indemnity to the trust property. The beneficial interests were to be evidenced solely by

[1] *Post*, p. —, Nos. 78-79. See, also, *post*, pp. —, —, No. 108, Swanson v. Commissioner, and No. 238, Helvering v. Combs.

transferable certificates for shares which were divided into 2,000 preferred shares of the par value of $100 each, and 2,000 common shares of no par value, and the rights of the respective shareholders in the surplus, profits, and capital assets were defined. "Share ledgers" showing the names and addresses of shareholders were to be kept.

The trustees might convene the shareholders in meeting for the purpose of making reports or considering recommendations, but the votes of the shareholders were to be advisory only. The death of a trustee or of a beneficiary was not to end the trust, which was to continue for twenty-five years unless sooner terminated by the trustees.

During the years 1921 and 1922, the trustees sold beneficial interests and paid commissions on the sales. About 42 acres (of the 155 acres described by the declaration of trust) were plotted into lots which were sold during the years 1921 to 1923, most of the sales being on the installment basis. On the remaining property a golf course and club house were constructed, and in 1923 this property with the improvements was conveyed to Western Avenue Golf Club, Inc., a California corporation, in exchange for its stock. Under a lease from the corporation petitioners continued the operation of the golf course until January 12, 1924. After that date petitioners' activities were confined to collections of installments of principal and interest on contracts of purchase, the receipt of interest on bank balances and of fees on assignments by holders of purchase contracts, the execution of conveyances to purchasers, the receipt of dividends from the incorporated club, and the distribution of moneys to the holders of beneficial interests. On December 31, 1923, the total number of outstanding beneficial interests was 3016 held by 920 persons; by December 31, 1926, the number of interests had been gradually decreased to 2172, held by 275 persons. The holdings by the trustees ranged approximately from 16 to 29 per cent.

Petitioners contend that they are trustees "of property held in trust", within section 219 of the Revenue Acts of 1924 and 1926,[2] and are taxable accordingly and not as an "association". They urge that, to constitute an association, the applicable test requires "a quasi-corporate organization in which the beneficiaries, whether or not certificate holders, have some voice in the manage-

[2] 43 Stat. 275; 44 Stat. 32.

ment and some control over the trustees and have an opportunity to exercise such control through the right to vote at meetings"; and that, in any event, the activities in which petitioners were engaged, during the tax years under consideration, did not constitute "a carrying on of business" within the rule applied by this court.

The Government insists that the distinction between associations and the trusts taxed under section 219 is between "business trusts on the one side" and other trusts "which are engaged merely in collecting the income and conserving the property against the day when it is to be distributed to the beneficiaries"; that Congress intended that all "business trusts" should be taxed as associations.

1. The Revenue Acts of 1924 and 1926 provided:

"The term 'corporation' includes associations, joint-stock companies, and insurance companies". (1924, sec. 2(a)(2); 1926, sec. 2 (a)(2)).[3]

A similar definition is found in the earlier Revenue Acts of 1917 (sec. 200), 1918 (sec. 1), and 1921 (sec. 2 (2)),[4] and also in the later Acts of 1928 (sec. 701 (a)(2)), 1932 (sec. 1111 (a)(2)), and 1934 (sec. 801 (a)(2)).[5]

The Corporation Tax Act of 1909,[6] which imposed an excise tax upon the privilege of doing business in a corporate capacity, embraced associations having a capital stock represented by shares and "organized under the laws of the United States or of any State or Territory". *Flint* v. *Stone Tracy Co.*, 220 U. S. 108, 144; *Eliot* v. *Freeman*, 220 U. S. 178, 186. The Income Tax Act of 1913,[7] taxed the net income of "every corporation, joint-stock company or association, and every insurance company, organized in the United States, no matter how created or organized, not including partnerships". The case of *Crocker* v. *Malley*, 249 U. S. 223, arose under the latter Act. The Court found that the declaration of trust in that case, relating to mill property, was on its face "an ordinary real estate trust of the kind familiar in Massachusetts", and that the function of the trustees was "not to manage the mills but simply to collect the rents and income of

[3] 43 Stat. 253; 44 Stat. 9.
[4] 40 Stat. 302; 40 Stat. 1058; 42 Stat. 227.
[5] 45 Stat. 878; 47 Stat. 280; 48 Stat. 771.
[6] 36 Stat. 112.
[7] 38 Stat. 172.

such property as may be in their hands, with a large discretion in the application of it, but with a recognition that the receipt holders are entitled to it subject to the exercise of the powers confided to the trustees". The Court thought that, if it were assumed that the words "no matter how created or organized" applied to "association", still it would be "a wide departure from normal usage" to call the beneficiaries a joint-stock association when they were not partners and had "no joint action or interest and no control over the fund". Nor could the trustees "by themselves" be treated as a joint-stock association within the meaning of the Act "unless all trustees with discretionary powers are such". *Id.*, pp. 232-234.

The decision in *Crocker* v. *Malley* was rendered in March, 1919, and the Treasury Department thereupon assumed that the degree of control exercised by the beneficiaries over the management of the trust was determinative of the question whether the trust constituted an "association". See statement of the rulings of the Bureau by the Board of Tax Appeals in *Woodrow Lee Trust* v. *Commissioner*, 17 B. T. A., pp. 111, 112. It was in that view, that the Regulations under the Revenue Acts of 1918 and 1921, in distinguishing an "association" from a "trust", provided as follows:

"If, however, the *cestuis que trust* have a voice in the conduct of the business of the trust, whether through the right periodically to elect trustees or otherwise, the trust is an association within the meaning of the statute". Regulations Nos. 45, 62, Art. 1504.

This ruling continued until our decision in May, 1924, in *Hecht* v. *Malley*, 265 U. S. 144, and furnished the test which the Board of Tax Appeals ~~theretofore~~ applied.[8] Accordingly, the Board in the case now before us, holding that under the trust instrument the shareholders "had no control over the trustees or the management of the business"; determined that the trust was taxable as such, and not as an association, for the years 1921, 1922 and 1923.

The case of *Hecht* v. *Malley* related to the excise taxes imposed upon "associations" by the Revenue Acts of 1916 (sec. 407) and 1918 (sec. 1000 (a)).[9] The provision of the Act of 1916 retained the qualifying words of the Corporation Tax Act of 1909—"organized under the laws of the United States, or any State or Terri-

[8] E. A. Landreth Co., 15 B. T. A. 655; Van Cleave Trust, 18 B. T. A. 486; Commercial Trust Co., 18 B. T. A. 1248; Rollin S. Sturgeon, et al., Trustees, 25 B. T. A. 368; Twin Bell Oil Syndicate, 26 B. T. A. 165.

[9] 39 Stat. 789; 40 Stat. 1126.

> In its determinations for earlier years.

tory"—and the Court followed the construction placed upon those words in *Eliot* v. *Freeman, supra.* But the Act of 1918 omitted this qualification and the excise tax as laid upon corporations applied to "associations" under the general definition. The Court thus found the terms of the Act of 1918 to be in significant contrast to the provisions of the Acts of 1909 and 1916. The omission of the qualification showed the intention of Congress "to extend the tax from one imposed solely upon organizations exercising statutory privileges, as theretofore, to include also organizations exercising the privilege of doing business as associations at the common law". 265 U. S. p. 155. Shorn of the restriction, the word "association" appeared to be used in its ordinary meaning, and we referred to several definitions found in standard dictionaries, as, *e. g.*, "a body of persons united without a charter, but upon the methods and forms used by incorporated bodies for the prosecution of some common enterprise"; "a body of persons organized, for the prosecution of some purpose, without a charter, but having the general form and mode of procedure of a corporation"; "an organized but unchartered body analogous to but distinguished from a corporation". *Id.*, p. 157. We expressed the view that the word "association", as used in the excise tax provision of the Revenue Act of 1918, clearly included "Massachusetts trusts", of the sort there involved, "having quasi-corporate organizations under which they are engaged in carrying on business enterprises". We were careful to say that it was then unnecessary to determine "what other form of 'associations', if any", the Act embraced. *Id.*

In the *Hecht* case, the trustees of the Hecht and Haymarket trusts relied strongly upon the decision in *Crocker* v. *Malley* as conclusively determining that those trusts could not be held to be associations, unless the trust agreements vested "the shareholders with such control over the trustees as to constitute them more than strict trusts within the Massachusetts rule". Reviewing the reasoning of that decision, we pointed out that it was not authority for the broad proposition advanced. We concluded that, when the nature of the trusts was considered, as the petitioners were "not merely trustees for collecting funds and paying them over," but were "associated together in much the same manner as the directors in a corporation for the purpose of carrying on business enterprises", the trusts were to be deemed associations within the

meaning of the Act of 1918. This was true "independently of the large measure of control exercised by the beneficiaries". And we rejected the view that Congress intended that organizations of that character "should be exempt from the excise tax on the privilege of carrying on their business merely because such a slight measure of control may be vested in the beneficiaries that they might be deemed strict trusts within the rule established by the Massachusetts courts".

Following this decision, the Treasury Department amended its regulation so as to provide that the distinction between an association and a trust should no longer depend upon beneficiary control. The new provision read:

"Operating trusts, whether or not of the Massachusetts type, in which the trustees are not restricted to the mere collection of funds and their payments to the beneficiaries, but are associated together in much the same manner as directors in a corporation for the purpose of carrying on some business enterprise, are to be deemed associations within the meaning of the Act, regardless of the control exercised by the beneficiaries". Regulations No. 65, Art. 1504, issued in October, 1924, under the Revenue Act of that year.

This provision was amended in August, 1925, so as to read as follows:

"If, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists within the meaning of section 2. Even in the absence of any control by the beneficiaries, where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the statute". T. D. 3748, IV-2 Cumulative Bulletin 7.

The text of the regulations relating to associations, so far as pertinent here, promulgated under the Act of 1924, is set forth in the margin. Regulations No. 65, Arts. 1502, 1504, as amended.[10]

[10] "Art. 1502. *Association.*—Associations and joint-stock companies include associations, common law trusts, and organizations by whatever name known, which act or do business in an organized capacity, whether created under and pursuant to State laws, agreements, declarations of trust, or otherwise, the net income of which, if any, is distributed or distributable among the shareholders on the basis of the capital stock which each holds, or, where there is no capital stock, on the basis of the proportionate share or capital

These regulations were continued substantially unchanged under the Revenue Acts of 1926 and 1928. No. 69, Arts. 1502, 1504; No. 74, Arts. 1312, 1314. The corresponding regulations under the Act of 1932 were somewhat modified, No. 77, Art. 1314; and these were considerably expanded by the regulations issued under the Act of 1934, No. 86, Art. 801-2, 801-3.

2. As the statute merely provided that the term "corporation" should include "associations", without further definition, the Treasury Department was authorized to supply rules for the enforcement of the Act within the permissible bounds of administrative construction. Nor can this authority be deemed to be so restricted that the regulations, once issued, could not later be clarified or enlarged so as to meet administrative exigencies or conform to judicial decision. Compare *Murphy Oil Company* v. *Burnet*, 287 U. S. 299, 303-307. We find no ground for the contention that by the enactment of the Revenue Act of 1924 the Department was limited to its previous regulations as to associations. And, while the case of *Hecht* v. *Malley* was concerned with the special excise tax provision of the Revenue Act of 1918, the ruling of the Court that the degree of the control by beneficiaries was not a decisive test in that relation could by similar reasoning be applied to the general income taxes laid by the revenue acts upon corporations and thus upon associations. These general income taxes covered both those taxes which in their nature were excise taxes on business, and as such could have been laid prior to the Sixteenth Amendment, and those taxes on other income which were permitted by that Amendment. *Stanton* v. *Baltic Mining Company*, 240 U. S.

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which each has or has invested in the business or property of the organization. . . ."

"Art. 1504. *Association distinguished from trust.*—Where trustees merely hold property for the collection of the income and its distribution among the beneficiaries of the trust, and are not engaged, either by themselves or in connection with the beneficiaries, in the carrying on of any business, and the beneficiaries have no control over the trust although their consent may be required for the filling of a vacancy among the trustees or for a modification of the terms of the trust, no association exists, and the trust and the beneficiaries thereof will be subject to tax as provided by section 219 and by articles 341-347. If, however, the beneficiaries have positive control over the trust, whether through the right periodically to elect trustees or otherwise, an association exists within the meaning of section 2. Even in the absence of any control by the beneficiaries, where the trustees are not restricted to the mere collection of funds and their payment to the beneficiaries, but are associated together with similar or greater powers than the directors in a corporation for the purpose of carrying on some business enterprise, the trust is an association within the meaning of the statute".

103, 107, 114. We think that the Department did not exceed its powers in rewriting its regulation, in the light of the decision in *Hecht* v. *Malley*, so as to provide with respect to the income taxes, in general, to be paid by associations, that the extent or lack of control by the beneficiaries of a trust should not in itself determine whether there was an association within the meaning of the statute. That the revised regulation had congressional approval is persuasively evidenced by the fact that the regulation, as amended in 1925, was continued without substantial alteration until 1933, and meanwhile Congress reenacted without change the general provision as to associations in the Revenue Acts of 1926, 1928, and 1932. See *Brewster* v. *Gage*, 280 U. S. 327, 337; *McCaughn* v. *Hershey Chocolate Co.*, 283 U. S. 488, 492; *Murphy Oil Company* v. *Burnet, supra; Helvering* v. *Bliss*, 293 U. S. 144, 151.

The question is not one of the power of Congress to impose this tax upon petitioners but is simply one of statutory construction,—whether Congress has imposed it. See *Burk-Waggoner Oil Association* v. *Hopkins*, 269 U. S. 110, 114. The difficulty with the regulations as an exposition was that they themselves required explication; that they left many questions open with respect both to their application to particular enterprises and to their validity as applied. The so-called "control test" had led to much litigation, and the change in the regulations after the decision in *Hecht* v. *Malley* caused increased uncertainty. That situation is put in a strong light by the action of Congress, in order to afford relief to taxpayers, in enacting section 704 of the Revenue Act of 1928 as a "retroactive" provision applicable, as stated, to trust returns which had been filed for a taxable year prior to 1925 under previous regulations and rulings, and also by giving an option to a trustee, in specified circumstances, in relation to the Revenue Act of 1926 and prior Acts.[11] While it is impossible in the nature of things to translate the statutory concept of "association" into a particularity of detail that would fix the status of every sort of enterprise or organization which ingenuity may create, the recurring disputes emphasize the need of a further examination of the congressional intent.

3. "Association" implies associates. It implies the entering into a joint enterprise, and, as the applicable regulation imports, an enterprise for the transaction of business. This is not the

[11] 45 Stat. 880.

characteristic of an ordinary trust—whether created by will, deed, or declaration—by which particular property is conveyed to a trustee or is to be held by the settlor, on specified trusts, for the benefit of named or described persons. Such beneficiaries do not ordinarily, and as mere *cestuis que trust*, plan a common effort or enter into a combination for the conduct of a business enterprise. Undoubtedly the terms of an association may make the taking or acquiring of shares or interests sufficient to constitute participation, and may leave the management, or even control of the enterprise, to designated persons. But the nature and purpose of the cooperative undertaking will differentiate it from an ordinary trust. In what are called "business trusts" the object is not to hold and conserve particular property, with incidental powers, as in the traditional type of trusts, but to provide a medium for the conduct of a business and sharing its gains. Thus a trust may be created as a convenient method by which persons become associated for dealings in real estate, the development of tracts of land, the construction of improvements, and the purchase, management and sale of properties; or for dealings in securities or other personal property; or for the production, or manufacture, and sale of commodities; or for commerce, or other sorts of business; where those who become beneficially interested, either by joining in the plan at the outset, or by later participation according to the terms of the arrangement, seek to share the advantages of a union of their interests in the common enterprise.

The Government contends that such an organized community of effort for the doing of business presents the essential features of an association. Petitioners stress the significance of, and the limitations said to be implied in, the provision classifying associations with corporations.

4. The inclusion of associations with corporations implies resemblance; but it is resemblance and not identity. The resemblance points to features distinguishing associations from partnerships as well as from ordinary trusts. As we have seen, the classification cannot be said to require organization under a statute, or with statutory privileges. The term embraces associations as they may exist at common law. *Hecht v. Malley, supra.* We have already referred to the definitions, quoted in that case, showing the ordinary meaning of the term as applicable to a body of persons united without a charter "but upon the methods and forms used

by incorporated bodies for the prosecution of some common enterprise." These definitions, while helpful, are not to be pressed so far as to make mere formal procedure a controlling test. The provision itself negatives such a construction. Thus unincorporated joint-stock companies have generally been regarded as bearing the closest resemblance to corporations. But, in the revenue acts, associations are mentioned separately and are not to be treated as limited to "joint-stock companies", although belonging to the same group. While the use of corporate forms may furnish persuasive evidence of the existence of an association, the absence of particular forms, or of the usual terminology of corporations, cannot be regarded as decisive. Thus an association may not have "directors" or "officers", but the "trustees" may function "in much the same manner as the directors in a corporation" for the purpose of carrying on the enterprise. The regulatory provisions of the trust instrument may take the place of "by-laws". And as there may be, under the reasoning in the *Hecht* case, an absence of control by beneficiaries such as is commonly exercised by stockholders in a business corporation, it cannot be considered to be essential to the existence of an association that those beneficially interested should hold meetings or elect their representatives. Again, while the faculty of transferring the interests of members without affecting the continuity of the enterprise may be deemed to be characteristic, the test of an association is not to be found in the mere formal evidence of interests or in a particular method of transfer.

What, then, are the salient features of a trust—when created and maintained as a medium for the carrying on of a business enterprise and sharing its gains—which may be regarded as making it analogous to a corporate organization? A corporation, as an entity, holds the title to the property embarked in the corporate undertaking. Trustees, as a continuing body with provision for succession, may afford a corresponding advantage during the existence of the trust. Corporate organization furnishes the opportunity for a centralized management through representatives of the members of the corporation. The designation of trustees who are charged with the conduct of an enterprise,—who act "in much the same manner as directors"—may provide a similar scheme, with corresponding effectiveness. Whether the trustees are named in the trust instrument with power to select successors, so as to constitute a self-perpetuating body, or are selected by, or

with the advice of, those beneficially interested in the undertaking, centralization of management analogous to that of corporate activities may be achieved. An enterprise carried on by means of a trust may be secure from termination or interruption by the death of owners of beneficial interests and in this respect their interests are distinguished from those of partners and are akin to the interests of members of a corporation. And the trust type of organization facilitates, as does corporate organization, the transfer of beneficial interests without affecting the continuity of the enterprise, and also the introduction of large numbers of participants. The trust method also permits the limitation of the personal liability of participants to the property embarked in the undertaking.

It is no answer to say that these advantages flow from the very nature of trusts. For the question has arisen because of the use and adaptation of the trust mechanism. The suggestion ignores the postulate that we are considering those trusts which have the distinctive feature of being created to enable the participants to carry on a business and divide the gains which accrue from their common undertaking,—trusts that thus satisfy the primary conception of association and have the attributes to which we have referred, distinguishing them from partnerships. In such a case, we think that these attributes make the trust sufficiently analogous to corporate organization to justify the conclusion that Congress intended that the income of the enterprise should be taxed in the same manner as that of corporations.

5. Applying these principles to the instant case, we are of the opinion that the trust constituted an association. The trust was created for the development of a tract of land through the construction and operation of golf courses, club houses, etc. and the conduct of incidental businesses, with broad powers for the purchase, operation and sale of properties. Provision was made for the issue of shares of beneficial interests, with described rights and priorities. There were to be preferred shares of the value of $100 each and common shares of no par value. Thus those who took beneficial interests became shareholders in the common undertaking to be conducted for their profit according to the terms of the arrangement. They were not the less associated in that undertaking because the arrangement vested the management and control in the trustees. And the contemplated development of the tract of land held at the outset, even if other properties were not acquired, involved what was essentially a business enterprise. The arrange-

ment provided for centralized control, continuity, and limited liability, and the analogy to corporate organization was carried still further by the provision for the issue of transferable certificates.

Under the trust, a considerable portion of the property was surveyed and subdivided into lots which were sold and, to facilitate the sales, the subdivided property was improved by the construction of streets, sidewalks and curbs. The fact that these sales were made before the beginning of the tax years here in question, and that the remaining property was conveyed to a corporation in exchange for its stock, did not alter the character of the organization. Its character was determined by the terms of the trust instrument. It was not a liquidating trust; it was still an organization for profit, and the profits were still coming in. The powers conferred on the trustees continued and could be exercised for such activities as the instrument authorized.

6. Petitioners contend that the trust was not taxable as an association, by reason of the retroactive provisions of section 704 (a) of the Revenue Act of 1928.[12] The contention is plainly unavailing and does not require an extended discussion. Section 704 (a) of the Act of 1928 provides, in substance, that where a taxpayer filed a return as a trust for a taxable year prior to 1925, the taxpayer shall be taxable as a trust, and not as a corporation, if the taxpayer was considered to be so taxable either (1) under the regulations in force at the time the return was made, or (2) under a departmental ruling then applicable and in force. Prior to the time for filing petitioners' return for the year 1924 the regulations had been amended, following the decision in *Hecht* v. *Malley, supra,* so as to provide that operating trusts in which the trustees were not restricted to the mere collection of funds and their payment to beneficiaries, but were associated together in much the same manner as directors in a corporation for the purpose of carrying on a business enterprise, should be deemed to be associations, regardless of the control exercised by the beneficiaries. Treasury Regulations No. 65, Art. 1504, October, 1924. It does not appear that there were regulations or rulings in force, at the time of the return for the taxable year 1924, under which the trust in this instance would be taxable as a trust and not as an association.

The judgment is affirmed.

Affirmed.

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[12] 45 Stat. 880.